

STATE OF CALIFORNIA
DEPARTMENT OF INSURANCE
45 Fremont Street, 21st Floor
San Francisco, California 94105

File No. RH02023676
Notice File No. Z-02-1021-03
Date: October 28, 2003

Subject: Regulations for Enforcement Actions and Penalties

FINAL STATEMENT OF REASONS

UPDATE OF INFORMATIVE DIGEST

The Commissioner has determined that the relevant considerations of detrimental impact and severity should be considered as part of the “nature” criterion rather than as separate criteria. This change was made because the “nature” of the violation is a specifically enumerated criterion in Insurance Code section 12921.1. As the detrimental impact and the severity of the violation are still part of the “nature” of the violation, this change has does not alter the effect of the proposed action.

The hypothetical violation examples were removed from the text before the Notice of Proposed Action and Notice of Public Hearing was issued. The hypothetical violation examples were never in the original text.

UPDATE OF INITIAL STATEMENT OF REASONS

On August 22, 2003, the Department of Insurance made available for public inspection certain changes to the regulation text as initially proposed. The changes were sufficiently related to the rulemaking as originally noticed such that a reasonable member of the directly affected public could have determined from the original notice that these changes could have resulted. Each substantive change is listed below, in the same order as those changes appear in the regulation.

The text of the proposed regulation has been divided into subdivisions and paragraphs have been renumbered for ease of reference. Each of these changes is nonsubstantial, in that they do not materially alter the requirements, rights, responsibilities, conditions or prescriptions contained in the original text. (Cal.Code Regs., tit. 1, §40.)

Section 2591. Preamble.

The new language is now divided into subdivisions, which are expressly designated (a) and (b). Also, the new language replaces the “and” with “or” in “violations of statutes ~~and~~or regulations”. The changes were made to provide clarity and to make the regulation easier to read. Each of these changes is nonsubstantial, in that they do not materially alter the requirements, rights, responsibilities, conditions or prescriptions contained in the original text. (Cal.Code Regs., tit. 1, § 40.)

The new language in subdivision (b) describes with more specificity the distinction between an

“enforcement action” and certain common activities such as market conduct exams, Department investigations and the like. This new language is reasonably necessary because more than one commenter expressed confusion about whether a market conduct examination was an “enforcement action” under our regulations. The new language, in conjunction with the new language in section 2591.1 (b), will clarify the distinction between an enforcement action and a market conduct examination.

Section 2591.1. Scope and Purpose.

One change that is noted throughout this regulation is the deletion of the word “commissioner” and insertion of the word “Department.” This change is reasonably necessary because it clarifies the manner in which enforcement actions, penalties and settlements are actually conducted by the Department. This distinction is explained in more detail below.

Specifically, the Department is the entity that is routinely charged with the task of conducting enforcement actions and negotiating settlements. The commissioner, in his or her capacity as the top official of the Department, is charged with the task of approving any final settlement agreement. (Cal.Ins.Code, § 12921(b)(1).) Whenever an enforcement action cannot be resolved through a settlement, the Department proceeds to an administrative hearing, and the commissioner acts as the ultimate arbiter of the facts and legal issues presented at the hearing. (See, e.g., Cal.Gov.Code, § 11517; Cal.Ins.Code, § 1861.08(c).) Therefore, the new language of this regulation was changed to reflect that it is the “Department,” rather than the “commissioner” that will actually be conducting enforcement actions and negotiating the settlement of those actions through the imposition of penalties.

Section 2591.1, Subdivisions (a) and (b).

The new language of subdivision (b), in conjunction with Section 2591 (b) describes with greater specificity the distinction between an “enforcement action” and certain common activities such as market conduct examinations, Department investigations, warning letters and the like. This new language is reasonably necessary because more than one commenter expressed confusion about whether a market conduct examination was an “enforcement action” under our regulations.

The new language will clarify the distinction between an enforcement action and a market conduct examination. The definition of enforcement action has been broadened to include actions in addition to those initiated through a formal pleading document. The definition now includes those actions that are settled through a Stipulation and Consent Order, or other less-formal settlement document. This change is reasonably necessary because there are circumstances where a settlement can occur without the filing of a formal document. In fact, the language of Insurance Code section 12921.1(a)(7) encompasses any imposition of penalty, without reference as to whether there has been a formal settlement document.

Section 2591.1, Subdivision (d).

The new language of subdivision (d) provides greater clarity to the reader, in that the regulations are not intended to be used by an administrative law judge, or at an administrative hearing. This change of language is simply a restatement of the previous language, in more specific terms. This new language provides that the regulations are intended for use in negotiating a settlement, but not for use by a trier of fact. This new language is reasonably necessary because it provides a

clearer statement of intent to the reader, when compared to the previous language.

Section 2591.2

The new language in this section is added “[I]f after a review of those criteria the Department determines that an enforcement action is warranted, the Department shall take into consideration the criteria listed in Section 2591.3 and any other relevant considerations to determine an appropriate penalty....” This change was reasonably necessary to provide clarity and achieve internal consistency as to how the regulation is applied. Further, the addition of “any other relevant considerations” is necessary to make the language consistent with section 2591.4(c) which states, in part, “...the Department may, in circumstances it deems appropriate, consider matters not listed in Section 2591.3.”

The new language at the end of this section added “including but not limited to attorneys’ fees.” This change was reasonably necessary so that the Department would not be disadvantaged by taking the more efficient settlement approach rather than forcing an action into the formal hearing process, where costs may be recoverable. There is statutory authority for recovery of costs, including attorney’s fees. (Cal.Ins.Code, § 12921(b)(4).) This addition is therefore reasonably necessary in order to carry out the intent of section 12921.1(a)(7) that the Commissioner establish a program listing these criteria and guidelines.

Section 2591.3, Subdivision (a)

The new language of subdivision (a) has deleted the language “detrimental impact, and the severity of the impact, resulting from” and inserted “nature of” the violation. The relevant considerations of detrimental impact and severity should be considered as part of the “nature” criterion rather than separate criteria. This change was reasonably necessary because “nature” of the violation is a specifically enumerated criterion in Insurance Code section 12921.1. As the detrimental impact and the severity of the violation are still part of the “nature” of the violation, this change does not alter the effect of the proposed action.

Section 2591.3, Subdivision (b)

The new language of subdivision (b) inserted the language “[s]everity of the violation includes...the extent of harm revealed through a consumer complaint or otherwise brought to the attention of the Department.” This change was reasonably necessary as the ultimate purpose of insurance regulation is to protect the public from harm. Whether the statute violated relates to claims handling, rating, underwriting, fraudulent business practices, or other regulated activity, the violation does not occur in a vacuum. Violations may severely impact the lives or businesses of those affected. The Department does not have the resources to prosecute every violation of the Insurance Code. When making a decision as between which of two insurers it will prosecute first or at all, where all other things are essentially equal, it is inconceivable that the Department would not take into consideration the extent of harm caused by the violations. Therefore, failing to include the extent of harm in these regulations may have precluded the Department from considering the extent of harm at any time when determining whether to bring an enforcement action.

Further, the Preamble of the regulation text explicitly points out that the statute requiring these

regulations “pertains to violations of statutes or regulations which are discovered in the investigation of consumer complaints.” As such, harm to the consumer, as reported in these complaints, should figure prominently in the criteria and guidelines the Department is required to develop. Therefore, this change was also reasonably necessary to carry out the intent of Section 12921.1(a)(7).

Section 2591.3, Subdivision (d)

It has been reasonably necessary for purposes of clarity to revise certain language describing the knowledge or willfulness criterion. Specifically, in subparagraph (d)(1)(A) a potential issue with circular reasoning has been addressed. Formerly, one of the specifically identified ways in which a violation would “be considered willful or knowingly committed” was “[w]hen the insurer knowingly acts in violation of the law.” Since the use of the term “knowingly” to describe behavior referred to as “knowing” was potentially confusing, the phrase “knowingly acts in violation” has been replaced with the following language: “is aware at the time of the act that it is violating.”

In paragraph (d)(2), the words “knowledge or” have been inserted preceding the word willfulness. This change was necessary in order to make the meaning of the paragraph sufficiently clear. The former language left open the possibility of the unintended interpretation that willfulness, but not knowledge, on the part of their agents would be attributed to insurers. The insertion brings the paragraph into conformity with the remainder of the subdivision, which in all other instances refers to both knowledge and willfulness together.

In addition, the following language at the end of paragraph (d)(2) has been deleted: “or otherwise not in the interest of the insurer at the time the act is committed.” The deleted language had been intended to expand beyond the situation where an employee acts outside the scope of employment the exception to the rule articulated in the paragraph, namely, that knowledge or willfulness on the part of agents and contractors would be imputed to insurers (i.e., the employer, principal, etc.). However, it has been reasonably necessary to refine the language by which this exception was expressed, because as written the exception had the potential of swallowing the rule, so to speak. Under the former language violators could have argued that almost any violation fit within the exception, since it would seldom be in an insurer’s interest for its agent, employee or contract entity to violate the law and thus subject the insurer to enforcement action and penalty. Additionally, the deleted language could have promoted much unfruitful discussion in negotiations on the subject of whether an act was or was not in the interest of the insurer. In place of the deleted language, it was therefore necessary to insert the words “agency or contract,” so that the exception now extends only to acts committed “outside the scope of the employment, agency or contract.”

Section 2591.3, Subdivision (f)

The new language in subdivision (f)(5) has deleted the word “related.” This change was reasonably necessary to make clear that the commissioner is not limited to reviewing only a specific type of noncompliance when reviewing an insurer’s compliance history. This provides the commissioner with the necessary flexibility to put the violation into context with the overall compliance behavior of the insurer, which is particularly necessary in determining whether an

enforcement action is necessary to encourage future compliance by the insurer or whether the noncompliance was an aberration that, once corrected, is not likely to be repeated.

Further, this change was necessary to avoid any potential disagreement regarding whether a current action is or is not related to a previous action.

Section 2591.3, Subdivision (g)

The new language in subdivision (g) added the word “violations.” This new language was reasonably necessary to make clear that this section will not preclude a series of ongoing violations from being treated as more than one violation. Although the language in this subsection goes only to one criterion used in determining duration for purposes of whether to bring an enforcement action and the appropriate penalty and in no way provides that multiple violations will be treated as one single violation, the change was made for clarity.

Section 2591.4, Subdivision (a)

It has been reasonably necessary to insert at the end of subdivision (a) the following sentence: “Neither inapplicability of one or more criteria nor absence of harm shall mitigate the effect of any relevant criterion.” The new language is necessary in order to preempt the unintended interpretation, possible under the former language, that the mere absence of facts indicating one or more of the criteria set forth in Section 2591.3 should itself mitigate the effect of a criterion that, by virtue of the existence of affirmative facts satisfying that criterion, was relevant. Under this unintended interpretation, the regulations would have been rendered unduly burdensome in operation, since the Department would have been required to consider not only the facts actually present in a particular case but also the virtually unlimited universe of facts *not* present. The new language makes clear the intended meaning of the proposed regulations, namely, that each criterion is to operate independently of the others; either there are facts which render a criterion applicable and therefore potentially relevant, or there are no such facts, in which case the criterion can never be relevant. As the sentence that precedes the inserted language makes clear, only relevant criteria are to receive consideration.

It has been reasonably necessary to specifically include in the inserted sentence in subdivision (a) of Section 2591.4 “absence of harm,” along with inapplicability of other criteria, among those things which are not to mitigate the effect of any relevant criterion, in order to prevent the misinterpretation of new language added to subdivision (b) of Section 2591.3: Severity of the violation. Extent of harm has been added as an indicator of the severity of the violation criterion; however, in order for this indicator to be operative, there again must be facts affirmatively indicating harm. The inserted phrase in Section 2591.4 makes clear that absence of such facts, on the other hand, simply means that the extent of harm indicator is not triggered; it does not mean that a violation that otherwise satisfies the severity of the violation criterion is somehow to be considered less severe owing to there having been no showing of harm which would have triggered this indicator. Without the inserted phrase, insurers could be incentivized to commit violations in instances where there could be no such showing of harm, if they thought they could predict that such violations would not be subject to enforcement actions or stiff penalties. This is not the intent of the proposed regulations.

Section 2591.4, Subdivision (c)

In subdivision (c), the sentence allowing the Department to consider matters not listed in Section 2591.3 has been revised for purposes of clarity. Formerly, the language could have supported the inference that there are unlisted criteria whose existence the Department chooses not to disclose. The Department, according to the old language, was not “precluded” from considering such absent criteria. In fact, the Department has made every effort to include in the proposed regulations all the considerations that could ever affect the decisions as to whether to pursue an enforcement action and as to the appropriate penalty amount. The new language conveys, in an affirmative statement, the meaning that the Department may consider matters not listed in Section 2591.3 but avoids the unintended implication that the proposed regulations deliberately omit a criterion of which the Department is currently aware.

Also in subdivision (c) the language requiring the Department to disclose the basis of considerations not listed in Section 2591.3 has been revised. Such considerations are now to be “stated during *the course of any* settlement negotiations” rather than “during the settlement negotiations,” as the old language indicated. This modification is reasonably necessary in order to admit of the possibility that there may not be such negotiations in every case. Further, the revision rules out the formerly possible interpretation that the statement would need to be made during each meeting in the case of settlement negotiations that extend over multiple sessions.

Section 2591.4, Subdivision (d)

Finally, a sentence has been added to the end of subdivision (d) in order ensure that the implementation of the proposed regulations will not act to waive, limit or impede the deliberative process privilege or any other right of confidentiality currently afforded the Department by law. This change is reasonably necessary in order to avoid any such erosion of confidentiality protection. The potential of being compelled to disclose the contents of its decision making processes would serve to chill internal communications, and could serve to limit the necessary flexibility the regulations currently provide the Department in its efforts to consider thoroughly and fairly each unique factual scenario.

UPDATE OF MATERIAL RELIED UPON

No material other than that presented in the initial statement of reasons has been relied upon by the Department of Insurance.

MANDATE ON LOCAL AGENCIES OR SCHOOL DISTRICTS

The Department has made a determination that adoption, amendment or repeal of the regulation does not impose a mandate on local agencies or school districts. The regulation has nothing to do with local agencies or school districts; it neither requires nor prohibits action on their part.

ALTERNATIVES

The Department of Insurance has determined that no alternative would be more effective in

carrying out the purpose for which the regulation is proposed, or would be as effective and less burdensome to affected private persons than the proposed regulation. This regulation is designed to create criteria and guidelines for implementing enforcement actions and assessing penalties. Insurance Code section 12921.1, subdivision (a), paragraph (7), requires the Department to create this list of criteria and guidelines. The Department has determined that, to the extent that enforcement and penalty guidelines are required by statute, the guidelines should be applied towards all enforcement and penalty actions arising from the statutes listed in the reference note of each section of the regulation in order to ensure consistent enforcement. While the Department of Insurance received a number of comments from the public, none of the comments presented a reasonable alternative to the regulation. Likewise, the Department of Insurance believes there is no reasonable alternative. Because no conceivable alternative regulation would be less burdensome to affected private persons without necessarily hampering the effective implementation of Insurance Code section 12921.1, subdivision (a), paragraph (7), or would be more effective in carrying out the purpose of providing greater uniformity in enforcement and in the general assessment of penalties imposed upon insurers the Commissioner proposes this regulation for adoption.

SUMMARY OF AND RESPONSE TO OBJECTIONS OR RECOMMENDATIONS

A verbatim recital of each written and oral comment, objection, and/or recommendation received during the public comment period and the response to each is attached hereto.

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
<p>Jeffery J. Fuller, Pres. Association of California Insurance Companies; National Association of Independent Insurers 1121 L. Street Ste. 510 Sacramento, CA 95814</p> <p>December 17, 2002</p> <p>Oral Submission.</p>		<p>Mr. Chairman and Panel Members. I'm Jeff Fuller with the Association of California Insurance Companies. We are just recently affiliated with the National Association of Independent Insurers, so I'm appearing on behalf of both. And let me just note, Mr. Chairman, that we will be submitting a letter to you by e-mail this afternoon. That e-mail is really a neat feature. And it goes into exhaustive detail since it was written by Sam Sorich. You know, it's pages and pages. Let me -- he asked that -- NAI's policy is to testify at hearings, so he asked that I come down today, it being a slow news day in Sacramento, and we don't have much to do, anything to do with the budget, because I don't think the Department of Insurance is involved in that. Let me just hit maybe a couple of the highlights that will be explained in better detail in the letter that you will get in this afternoon. The first is, and apparently we are not the only one, apparently, although you don't have a lot of interest at the hearing, you have gotten some written comments.</p>	<p>The comment suggests that the Department lacks authority to make these regulations applicable to cases other than those that begin through the complaint investigation program described in Insurance Code section 12921.1. The Commissioner has considered the comment and rejects it.</p> <p>Subdivision (b) of proposed regulations section 2591 acknowledges that these regulations are intended to apply to more cases than simply those cases subject to Insurance Code section 12921.1(a)(7). Indeed, the Reference provision and section 2591.1 of the proposed regulations list the penalty provision statutes, which these regulations will implement, interpret and make specific. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department's authority to promulgate regulations which apply to other investigations of insurer conduct where the Department has inherent authority to implement its regulatory criteria.</p> <p>The penalty statutes listed in the Reference provision and section 2591.1 give the Commissioner authority to impose a penalty from within a range. For example, Insurance Code section 1858.07 authorizes the Commissioner to impose a penalty "not to exceed" \$5,000 for a non-willful violation and "not to exceed" \$10,000 if the violation is willful. Insurance Code section 12921, subdivision (a) requires the Commissioner to enforce the provisions of the Insurance Code and other laws relating to the business of insurance in this state. The Commissioner has inherent power to implement, interpret and make specific the manner in which these penalty ranges will be applied in practice.</p> <p><i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, "[The Commissioner's] powers are not limited to those</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>So one of the things I think is generally discussed by the insurers is that we believe that the department is going a little beyond the authority in adopting and promulgating these regulations. And as I say, I missed the conference call, but apparently there was some concern that the regulations are adopted pursuant to the insurance complaint handling program in that statute, the list of criteria to determine which violations should be pursued through enforcement actions. And I think the view of our companies is that the regulations ought to be limited to that narrow purpose. And I don't have specifics, but I'm told that -- I assume without knowing that many, perhaps most of the complaints you get involve claims handling. That's another set of regulations. And they said there are some discrepancies that perhaps could be worked out. But is it really necessary to have another set of regulations? You got your Fair Claims Practices regulations pretty well worked out. And so let's keep these regulations limited to this issue</p>	<p>expressly conferred by statute; “rather, “[it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.”” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (<i>Italics added.</i>)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute.</p> <p>Here, the proposed regulations will apply to statutes which authorize the Commissioner to seek a penalty “not to exceed” a certain amount. (See, e.g., Ins. Code sections 1858.07 & 10140.5.) It is necessary to promulgate regulations for settlement purposes insofar as the statutes referenced in the proposed regulations authorize the Commissioner to impose penalties within a range, and therefore the Commissioner has inherent authority to create a regulatory scheme to decide appropriate penalties within that range. Furthermore, each agency has inherent (as well as statutory) power to settle cases prior to a hearing, in a manner in which the parties see fit. (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114.)</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>about the criteria about when a consumer complaint is going to lead the department to go on to an enforcement action. I think that it in part was intended to give notice to consumers so they are not just calling with everything so they understand what it is that the department is looking for in order to pursue a complaint against an insurance company.</p>	<p><i>110, 114.)</i></p> <p>Government Code section 11415.60 recognizes that “[a]n agency may formulate and issue a decision by settlement, pursuant to an agreement of the parties, without conducting an adjudicative proceeding. Subject to subdivision (c), the settlement may be on any terms the parties determine are appropriate.” Subdivision (c) states, in part, “The terms of a settlement may not be contrary to statute or regulation, except that the settlement may include sanctions the agency would otherwise lack power to impose.”</p> <p>Therefore, the Commissioner has broad discretion to adopt rules and regulations as necessary to promote the public welfare. The proposed regulations concern a number of statutes that give the Commissioner the power to impose penalties within a range after a hearing, but the statutes are silent regarding where the appropriate penalty is within the range. We also know that agencies are empowered to settle cases prior to hearing, and that the settlement may include sanctions which do not violate public policy that the agency would otherwise lack the power to impose. It is reasonable for the Commissioner to conclude that, when settling cases, he will use the statutory penalty ranges as a guideline for deciding what sanctions to impose at settlement. Moreover, the Commissioner’s broad discretion to adopt rules and regulations that “may fairly be implied from the statute granting the powers” authorizes him to create guidelines/criteria for enforcement and penalty assessment. (See, generally, <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825.)</p> <p>The authority to adopt these regulations may be fairly implied from those statutes that recognize the agency’s inherent power to settle cases “on any terms the parties determine are appropriate.” Additionally, the authority to adopt these regulations may be fairly implied from those statutes that</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>to adopt these regulations may be fairly implied from those statutes that designate a penalty range that may be imposed after a hearing.</p> <p>To the extent that this comment suggests the proposed regulations duplicate, or are inconsistent with the Fair Claims settlement practices regulations, the Commissioner has considered and rejects the comment. The comment does not cite any specific examples where there is an inconsistency between the proposed regulations and the Fair Claims settlement practices regulations.</p> <p>At least one commenter has argued that the proposed regulations do not meet the necessity standard, in light of the fair claims settlement practices regulations. This comment has been considered and is rejected. First, in the context of consumer complaints, the proposed regulations are necessary because Insurance Code section 12921.1(a)(7) expressly requires that we promulgate them.</p> <p>As the commenter notes, however, the Department has decided to promulgate these regulations for use in conducting enforcement actions that are initiated for reasons other than consumer complaints. Examples of the kinds of situations where the proposed regulations would also apply include enforcement actions, which are based upon the findings of a market conduct examination or other Department investigation. Regardless of whether the Department conducts an enforcement action based upon the findings of a market conduct examination, a Department investigation, or in response to a consumer complaint, the decision regarding the appropriate penalty and whether to bring an enforcement action is the same. Therefore, the proposed regulations must cover more contexts than merely those cases where a consumer complaint has led to</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>an enforcement action. If the proposed regulations did not apply to the findings from market conduct examinations or investigations, this would raise a potential consistency problem. The regulations would be inconsistent because, by all accounts, enforcement actions and penalties are imposed in exactly the same way, regardless of whether they are initiated by a consumer complaint, the findings of a market conduct exam, or a Department investigation. Yet, by making the proposed regulations apply solely to consumer complaints, they could lead to inconsistent enforcement of actions, which arise under other circumstances. For the reasons mentioned above, the proposed regulations must necessarily apply to other situations where the Department discovers – through a market conduct exam, investigation, or other non-consumer-complaint context – that an enforcement action is needed.</p> <p>Contrary to this commenter’s suggestion, the proposed regulations are not intended to provide any instruction to consumers as to what the Department is looking for when a consumer files a consumer complaint. Instead, the proposed regulations are designed, in part, to make the Department’s criteria for deciding which enforcement actions to pursue and how much penalty to impose a transparent process. Because the Department of Insurance is a public agency, the Commissioner recognizes the value in allowing consumers and the industry a clear understanding of how the Department conducts its enforcement affairs. This is so that consumers and the insurance industry can monitor the actions of this agency and ensure that the Department of Insurance is carrying out the will of the voters and the Legislature. While it is possible that some consumers may use these regulations as a guideline when filing consumer complaints, they are not intended for that purpose.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(c)	<p>The other point, they have mentioned that they believe that there are some inconsistencies between these regs and the Fair Claims settlement practices regulations and that, you know, they get focused on those Fair Claims settlement practices regs and everybody started to learn them, and it has to filter all the way down through some pretty big organizations down to the working level. So they think that having another set of regulations, possibly inconsistent, possibly in conflict, but just another set of regulations is just one more piece of a complex puzzle that doesn't advance your regulatory purposes and it doesn't advance insurers being sure to comply with the law.</p> <p>Another part, and this was -- this will be laid out more in the letter too, is that they were bothered by a concept of willfulness. The concept of willfulness is different than the concept of knowledge. And imputing the specific intent to companies simply because they know of a practice to infer from that that they</p>	<p>Any inconsistencies with the Fair Claims Settlement Practices regulations are resolved by the following language in Section 2591.1 of the proposed regulations: "To the extent that the provisions of this article conflict with the provisions of any statute or other regulation that more specifically addresses a particular violation, this article shall be inapplicable." Nonetheless, there are no significant inconsistencies with the Fair Claims Settlement Practices regulations. The only possible area of overlap involves Cal. Code Regs, tit. 10, §2695.12, subds. (b) and (c). In subdivision (b), a list of the types of admissible evidence is provided which the Commissioner will consider in determining appropriate penalties. However, the list is not an exclusive list, and the kinds of evidence that according to the existing regulation are to be considered are indeed entirely consistent with the criteria set forth in the proposed regulations. Subdivision (c) indicates, in pertinent part, that in determining penalties to be assessed under the Unfair Claims Settlement Practices regulations, that the Commissioner "shall not consider reasonable mistakes or opinions as to valuation of property, losses or damages." Cal. Code Regs, tit. 10, §2695.11, subd. (c). It is conceivable that, in the claims valuation context only, this language could be at odds with Section 2591.3(d)(a)(B) of the revised text of regulations. If there were indeed an inconsistency, then Section 2591.1 of the proposed regulations makes it clear that the proposed regulations would be inapplicable, to the extent of the inconsistency, as noted above. However, it is by no means clear that "reasonable mistake[s]" such as those excepted from consideration under the existing regulations could ever be considered knowledgeable or willful under the proposed regulations for the reason that "the insurer reasonably should have known of the act's unlawfulness when the non-compliant act occurred." It seems logical that if the insurer</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>had the intent to violate the statutory provision they thought was unfair. So they thought that the willfulness concept ought to be – since it can lead to higher penalties, as you know, can lead to a lot of things, there is a big distinction between willfulness and knowledge, and that the willfulness should include the intent to basically commit a violation. That was one part of that.</p>	<p>the non-compliant act occurred.” It seems logical that if the insurer reasonably should have known of an act’s unlawfulness, then such an act could not fairly be considered a reasonable mistake.</p> <p>Further, the regulations impose no new requirements on insurers, which would need to filter down through an organization. Insurers will continue be charged with a degree of knowledge of the law sufficient to avoid violations of the Insurance Code, in the same way they currently are. The proposed regulations in no way alter what constitutes a violation.</p> <p>It is useful to note that the proposed regulations come into play only when an insurer has violated the law. The regulations presuppose that there has been a violation: “The Department shall examine the violations committed by the insurer” (Section 2591.2 of the amended text of the proposed regulations). The regulations do not change existing legal definitions of knowledge or willfulness, or blur the legal distinctions between these two concepts. The regulations merely indicate that, given there has already been a violation of the law, no such distinction will be made in the Department’s deliberations as to whether or not to take an enforcement action and as to the penalty amount.</p> <p>Existing law is utterly silent as to how the Department is to arrive at an exact penalty amount from within the applicable statutory range of penalty amounts. The proposed regulations in fact presuppose that a determination has been made, before the regulations become operative, as to which particular statutory penalty provisions apply: “the Department shall take into consideration the criteria ... to determine an appropriate penalty for each act in violation of the law</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>There is going to be a section in the</p>	<p>from within the applicable statutory penalty range or ranges (Section 2591.2 of the amended text of the proposed regulations). There can therefore be no inconsistency in this regard.</p> <p>The regulations reflect a choice by the Department that the exact nature or extent of guilty knowledge on the part of violators will not ordinarily be considered in the Department’s decision making process, once it has been established that a particular statute has been violated and that a particular penalty provision applies. Instead, the criteria listed in Section 2593.1 will form the basis of the Department’s determinations as to which violations will be pursued by enforcement actions. The legal distinctions between knowledge and willfulness will of course continue to be observed with regard to the determination of whether or not there has in fact been a violation in the first place, both by the Department and by the courts.</p> <p>Finally, the commenter questions the fairness of the proposed regulations. Specifically, the commenter objects to the inference of intent from mere knowledge. The regulations are entirely fair. Certainly they do nothing to limit insurers’ due process rights; should an insurer object to the operation of the proposed regulations, it is entitled to proceed to hearing, just as has always been the case. In addition, the inference complained of is not unfair in the sense that it is irrational. The Department has chosen in the proposed regulations to make the assumption that a knowing act also involves willfulness for the reason that the Department wished to discourage knowing violations of the Insurance Code.</p> <p>This comment makes reference to the “examples for penalties” portion of the regulation. The “examples for penalties” provision was presented as</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>letter, I have never seen this done, but there were some Objections to the notice of hearing. Now, I'm not even sure what the legal effect of that is, but the notice, because you made some changes in the regs in response to which, by the way, everybody appreciated because I think everybody went into a catatonic fit when they saw the examples for penalties and it's going to be 25, that shook everybody up. And Mr. Chairman, I'll be honest with you, I said in the one conversation I was in, I said I think what the department is trying to do is give everybody an idea, like sentencing guidelines in the spirit, of course. But we just met unanimous disapproval of that concept. They would rather just deal with the department on the market conduct examinations. You have all the discretion, the statutes are there to lay out your penalties, and they are just fine to deal with you on that basis. And I think most of those things are settled. So they were – they were very appreciative of getting rid of that appendix in the earlier</p>	<p>the regulation. The “examples for penalties” provision was presented as part of a request for public input hearing, conducted pursuant to Government Code section 11346.45. After the Department received significant input, which disapproved of this provision, the Department elected to remove the provision. Because this provision was not part of the regulation text, which was noticed for a rulemaking hearing, no response is necessary.</p> <p>The Commissioner has considered the comment and rejects it. Contrary to the suggestion stated in the comment, the Department did state that the proposed regulations may have a significant adverse economic impact on businesses. This was stated in the Department’s Notice of Proposed Action and Notice of Public Hearing. The comment also suggests that the significant adverse economic impact “should have been explained a little bit.” The Department did describe the possible significant adverse economic impact, in accordance with the requirements of Government Code section 11346.5.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>draft.</p> <p>In the notice, then they said this regulation you didn't put in may have a significant statewide adverse economic impact on businesses. I'm not sure why that's in there. That's one of these provisions that was stuck in the APA a thousand years ago, because you didn't go into the impact, but they thought that should have been explained a little bit. I don't know, in a way -- and I kind of argued with people about this. I think the notice is like Legislative Counsel's Digest On Legislation. It's not controlling, but it makes everybody nervous if it's out of synch with the regs. So they were a little bothered about the notice, and I don't know even what to recommend that you do about it. It was they thought inconsistent with the regs.</p> <p>So I think that's about all I have to say, Mr. Chairman. As I say, you will be getting a letter this afternoon. I think everybody really appreciates it when the department went to that e-</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		mail concept so that we could get these things off to you. I think you have gotten other written comments as well on that.	
Mark Webb State Relations Officer American International Group 175 Water Street, 18 th Fl. New York, NY 10038 December 17, 2002 Oral Submission.	2591.3 (c).	<p>I gave the reporter my card already, so he has the spelling. My name is Mark Webb, State Relations Officer with the American International Group. I really have only one brief comment to make, given the impending fire drill. This is in regards to the definition of willful conduct in proposed Section 2591.3, Subdivision C. Specifically, we think that as it relates to alleged violations of Section 11756 of the Insurance Code that the definition of willful conduct is already established in statute in Section 11750.1 Subdivision D, and that the expansion of the definition of willful beyond that contained in that statute goes beyond the authority of the Department of Insurance in this regulatory process.</p> <p>The other specific concern that we have in these particular regulations is that "Violations --" and I'm quoting</p>	<p>Any inconsistencies with the cited Insurance Code sections are resolved by the following language in Section 2591.1 of the proposed regulations: "To the extent that the provisions of this article conflict with the provisions of any statute or other regulation that more specifically addresses a particular violation, this article shall be inapplicable."</p> <p>The proposed regulations in no way expand the definition of what constitutes willful conduct for purposes of determining whether a violation of the Insurance Code has taken place.</p> <p>It is useful to note that the proposed regulations come into play only when an insurer has violated the law. The regulations do not change existing legal definitions of willfulness. The regulations merely indicate that, given there has already been a violation of the law, willfulness will be evaluated according to the language of the proposed regulations in the Department's deliberations as to whether or not to take an enforcement action and as to the penalty amount. Existing law is utterly silent as to how, given that a particular penalty provision is applicable, the Department is to arrive at an exact penalty amount from within the applicable statutory range of penalty amounts; there can therefore be no inconsistency in this regard.</p> <p>The language of the proposed regulations is clear. Further, the proposed regulations in no way alter the obligations of the regulated public. Insurers will continue be charged with a degree of knowledge</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>from the text here, "Violations that may be considered willful or knowingly committed include, but are not limited to, the following."When arguing the specific type of conduct may be willful, it would seem to me that the purpose of the regulation should be to clearly define what willful conduct is, and not leave it to a potential ad hoc determination at the time of the market conduct examination or of reviewing of complaint activity. And we would suggest that at least in practice, and maybe as a matter of construction of this regulation, that by suggesting that there will be other ways of determining willful conduct than that prescribed in the regulation that the regulation lacks the clarity that's necessary to allow the regulated public to understand their obligations under these new regulations. And that's it. Other than that, it's a fine regulation.</p>	<p>public. Insurers will continue be charged with a degree of knowledge of the law sufficient to avoid violations of the Insurance Code, in the same way they currently are. The proposed regulations in no way alter what constitutes a violation.</p> <p>The regulations reflect a choice by the Department that the exact nature or extent of guilty knowledge on the part of violators will not ordinarily be considered in the Department's decision making process, once it has been established that a particular statute has been violated. Instead, the criteria listed in Section 2593.1 will form the basis of the Department's determinations as to which violations will be pursued by enforcement actions. The existing legal definition of willfulness will of course continue to be observed with regard to the determination of whether or not there has in fact been a violation in the first place, both by the Department and by the courts.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
<p>Samuel Sorich Association of California Insurance Companies 1121 L Street, Suite 406 Sacramento, CA 95814-3943 December 17, 2002 Written Submission via e-mail</p>	2591 & 2591.1	<p><u>Sections 2591 and 2591.1 – Lack of Authority to Expand the Proposed Regulations Beyond Consumer Complaints</u></p> <p>The Department of Insurance’s notice of hearing on the proposed regulations states, “The purpose of the proposed regulation is to implement a statutory mandate.” That statutory mandate is in Insurance Code §12921.1(a)(7) which requires the insurance commissioner to establish a list of criteria for an enforcement action and possible penalties against an insurer when the enforcement action is initiated by a consumer complaint. The regulations acknowledge their foundation in §12921.1(a)(7) by citing the Insurance Code Section as authority for each of the proposed regulatory sections.</p> <p>The text of the regulations diverges from the statutory basis for the regulations. The statutory mandate in Insurance Code §12921.1(a)(7) calls for regulations which set forth criteria</p>	<p>The comment suggests that the Department lacks authority to make these regulations applicable to cases other than those that begin through the complaint investigation program described in Insurance Code section 12921.1. The Commissioner has considered the comment and rejects it.</p> <p>Subdivision (b) of proposed regulations section 2591 acknowledges that these regulations are intended to apply to more cases than simply those cases subject to Insurance Code section 12921.1(a)(7). Indeed, the Reference provision and section 2591.1 of the proposed regulations list the penalty provision statutes, which these regulations will implement, interpret and make specific. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department’s authority to promulgate regulations which apply to other investigations of insurer conduct where the Department has inherent authority to implement its regulatory criteria.</p> <p>The penalty statutes listed in the Reference provision and section 2591.1 give the Commissioner authority to impose a penalty from within a range. For example, Insurance Code section 1858.07 authorizes the Commissioner to impose a penalty “not to exceed” \$5,000 for a non-willful violation and “not to exceed” \$10,000 if the violation is willful. Insurance Code section 12921, subdivision (a) requires the Commissioner to enforce the provisions of the Insurance Code and other laws relating to the business of insurance in this state. The Commissioner has inherent power to implement, interpret and make specific the manner in which these penalty ranges will be applied in practice.</p> <p><i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, “[The Commissioner’s] powers are not limited to those</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>for enforcement actions and penalties that are initiated by consumer complaints. The first paragraph of proposed Section 2591 correctly states that the purpose of the regulations is to meet the requirements of Insurance Code §12921.1(a)(7) and then recognizes that §12921.1(a)(7) “pertains to violations of statutes and regulations which are discovered through the investigation of consumer complaints.” The second paragraph of the proposed Section 2591 goes beyond the statutory authority for the regulations by attempting to apply the regulations to actions that are not generated by consumer complaints. The application of the proposed regulations to enforcement actions that are not initiated by consumer complaints is not authorized.</p> <p>Similarly, proposed Section 2591.1 would apply the criteria in the proposed regulations to every instance where the insurance commissioner imposes any of the specified nineteen penalty sections in</p>	<p>expressly conferred by statute; “rather, “[it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.”” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (<i>Italics added.</i>)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute.</p> <p>Here, the proposed regulations will apply to statutes which authorize the Commissioner to seek a penalty “not to exceed” a certain amount. (See, e.g., Ins. Code sections 1858.07 & 10140.5.) It is necessary to promulgate regulations for settlement purposes insofar as the statutes referenced in the proposed regulations authorize the Commissioner to impose penalties within a range, and therefore the Commissioner has inherent authority to create a regulatory scheme to decide appropriate penalties within that range. Furthermore, each agency has inherent (as well as statutory) power to settle cases prior to a hearing, in a manner in which the parties see fit. (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114.)</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>the Insurance Code. The Legislature has not directed commissioner to establish criteria for penalties resulting from enforcement actions that are initiated by the Department. Applying the regulations' criteria to penalties for violations that are not discovered in the investigation of consumer complaints goes beyond the authority which the Legislature has granted to the insurance commissioner.</p> <p>The fundamental invalidity of the proposed regulations is their failure to comply with Government Code §11349.1 which requires regulations to be based on statutory authority. In order to stay within the scope of the authority granted by §12921.1(a)(7), proposed Sections 2591 and 2591.1 should be amended to limit the application of the regulations to enforcement actions and penalties arising from the investigation of consumer complaints.</p>	<p><i>110, 114.)</i></p> <p>Government Code section 11415.60 recognizes that “[a]n agency may formulate and issue a decision by settlement, pursuant to an agreement of the parties, without conducting an adjudicative proceeding. Subject to subdivision (c), the settlement may be on any terms the parties determine are appropriate.” Subdivision (c) states, in part, “The terms of a settlement may not be contrary to statute or regulation, except that the settlement may include sanctions the agency would otherwise lack power to impose.”</p> <p>Therefore, the Commissioner has broad discretion to adopt rules and regulations as necessary to promote the public welfare. The proposed regulations concern a number of statutes that give the Commissioner the power to impose penalties within a range after a hearing, but the statutes are silent regarding where the appropriate penalty is within the range. We also know that agencies are empowered to settle cases prior to hearing, and that the settlement may include sanctions which do not violate public policy that the agency would otherwise lack the power to impose. It is reasonable for the Commissioner to conclude that, when settling cases, he will use the statutory penalty ranges as a guideline for deciding what sanctions to impose at settlement. Moreover, the Commissioner’s broad discretion to adopt rules and regulations that “may fairly be implied from the statute granting the powers” authorizes him to create guidelines/criteria for enforcement and penalty assessment. (See, generally, <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825.)</p> <p>The authority to adopt these regulations may be fairly implied from those statutes that recognize the agency’s inherent power to settle cases “on any terms the parties determine are appropriate.” Additionally, the authority</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>to adopt these regulations may be fairly implied from those statutes that designate a penalty range that may be imposed after a hearing.</p> <p>To the extent that this comment suggests the proposed regulations duplicate, or are inconsistent with the Fair Claims settlement practices regulations, the Commissioner has considered and rejects the comment. The comment does not cite any specific examples where there is an inconsistency between the proposed regulations and the Fair Claims settlement practices regulations.</p> <p>At least one commenter has argued that the proposed regulations do not meet the necessity standard, in light of the fair claims settlement practices regulations. This comment has been considered and is rejected. First, in the context of consumer complaints, the proposed regulations are necessary because Insurance Code section 12921.1(a)(7) expressly requires that we promulgate them.</p> <p>As the commenter notes, however, the Department has decided to promulgate these regulations for use in conducting enforcement actions that are initiated for reasons other than consumer complaints. Examples of the kinds of situations where the proposed regulations would also apply include enforcement actions, which are based upon the findings of a market conduct examination or other Department investigation. Regardless of whether the Department conducts an enforcement action based upon the findings of a market conduct examination, a Department investigation, or in response to a consumer complaint, the decision regarding the appropriate penalty and whether to bring an enforcement action is the same. Therefore, the proposed regulations must cover more contexts than merely those cases where a consumer complaint has led to</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>an enforcement action. If the proposed regulations did not apply to the findings from market conduct examinations or investigations, this would raise a potential consistency problem. The regulations would be inconsistent because, by all accounts, enforcement actions and penalties are imposed in exactly the same way, regardless of whether they are initiated by a consumer complaint, the findings of a market conduct exam, or a Department investigation. Yet, by making the proposed regulations apply solely to consumer complaints, they could lead to inconsistent enforcement of actions, which arise under other circumstances. For the reasons mentioned above, the proposed regulations must necessarily apply to other situations where the Department discovers – through a market conduct exam, investigation, or other non-consumer-complaint context – that an enforcement action is needed.</p>
	2591.3	<p><u>Section 2591.3 – Inconsistency with Fair Claims Settlement Practices Regulations</u></p> <p>The regulations also cite Insurance Code §790.10 as authority. Insurance Code §790.10, which is in Article 6.5 of Chapter 1 of Part 2 of Division 1 of the Insurance Code, grants the insurance commissioner the power to promulgate regulations on unfair practices, including unfair claims practices. Under the authority</p>	<p>The Commissioner has considered the comment and respectfully rejects it. The commenter suggests that there is an inconsistency between the proposed regulations and the Fair Claims Settlement Practices regulations and urges that the proposed regulations be amended to exclude their applicability to noncompliance and penalties related to the Fair Claims Settlement Practices regulations. The commenter urges that different criteria are considered when comparing both of the above-mentioned regulations; however, the key difference is that the proposed regulations are used for settlement purposes, while the Fair Claims</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>granted by Insurance Code §790.10, the Department of Insurance has adopted the Fair Claims Settlement Practices Regulations which set forth criteria for determining noncompliance and appropriate penalties related to the claims practices standards established by the Regulations.</p> <p>In requiring the insurance commissioner to establish a program for handling consumer complaints, the Legislature directed the commissioner to make sure that the program's procedures are consistent with the specific procedures that are already in place for enforcing fair claims practices. Insurance Code §12921.1(a)(6) states that the consumer complaint procedures "shall be consistent with those in Article 6.5 (commencing with Section 790) of Chapter 1 of Part 2 of Division 1 for complaints within the purview of that article..." Applying the criteria in the proposed regulations to claims practices would create an inconsistency. Thus, the</p>	<p>regulations are not used specifically for settlement purposes and are used by Administrative Law Judges in administrative hearings. Therefore, the Department is not "pick[ing] and choos[ing]" which set of criteria it wishes to apply to an insurer's claims practices. Any such inconsistencies with the Fair Claims Settlement Practices regulations are resolved by the following language in Section 2591.1 of the proposed regulations: "To the extent that the provisions of this article conflict with the provisions of any statute or other regulation that more specifically addresses a particular violation, this article shall be inapplicable." Nonetheless, there are no significant inconsistencies with the Fair Claims Settlement Practices regulations.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>proposed regulations should be amended to exclude their applicability to noncompliance and penalties related to the Fair Claims Settlement Practices Regulations.</p> <p>Section 2695.12 of the Department's Fair Claims Settlement Practices Regulations sets forth criteria which the insurance commissioner is required to consider in determining whether an insurer has complied with the Regulations and if there is noncompliance, what penalty, if any, should be imposed. Proposed Section 2591.3 sets forth a different set of criteria. Therefore, if the proposed regulations are adopted in their current form, when the Department investigates an insurer for an alleged unfair claims practice, the insurer will not know what criteria the Department will use to determine noncompliance and to set penalties. Will penalties be guided by the criteria in the Fair Claims Settlement Practices Regulations, or will penalties be determined by the criteria in proposed Section 2591.3?</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>There are similarities between Section 2695.12 and proposed Section 2591.3, but there are also significant differences. For example, Section 2695.12(b)(7) requires the commissioner to consider the relative number of claims where the noncomplying acts are found to exist, as contrasted to the total number of claims handled by the insurer during the relative time period. Proposed section 2591.3(b) takes a different approach. The proposed regulation allows the commissioner to consider the number of violations within the insurer's claims population or among the claims population of the insurer's competitors. The Department's proposed November 7, 2002 amendments to Section 2695.12 would move even farther away from the criteria in proposed Section 2591.3. Under the November 7 amendments, the insurance commissioner would be required to consider the relative number of claims where violations are found to exist, as contrasted to the total</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>number of claims “reviewed by the Department for the relevant time period.” In addition, existing Section 2695.12(b)(3) <u>requires</u> the commissioner to consider the complexity of claims when the commissioner determines noncompliance and appropriate penalties. In contrast, proposed Section 2591.3(a)2 states “consideration <u>may</u> also be given to the necessary complexity of the transaction in determining the severity of the act.” (<i>emphasis added</i>)</p> <p>The Department does not have the right to “pick and choose” which set of criteria it wishes to apply to an insurer’s claims practices. Noncompliance and penalties for unfair claims practices are determined under the criteria set forth in the Fair Claims Settlement Practices Regulations. In order to comply with the Legislature’s mandate in Insurance Code §12921.1(a)(6) for regulatory consistency, the enforcement and penalty criteria in the proposed regulations should not</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(a)	<p>be applied to insurer claims practices.</p> <p><u>Section 2591.3 – Comments on Criteria</u></p> <p><i>Section 2591.3(a) - Detriment and Severity</i></p> <p>The proposed regulations’ description of detrimental impact and severity of impact include claims issues which, as explained above, should be deleted from the proposed regulations’ criteria.</p>	<p>The Commissioner has considered the comment and respectfully rejects it. §12921.1(a)(7) requires the commissioner to establish a list of criteria to determine which violations should be pursued by enforcement action and enforcement guidelines that set forth appropriate penalties for violations. A consumer complaint may involve claims issues and there is nothing preventing the commissioner from considering claims issues as part of the determination of detrimental impact and severity of impact. In the alternative, if the commenter is referring to the Fair Claims Settlement Practices Regulations then the proposed regulations cannot be duplicative or inconsistent with the Fair Claims Settlement Practices Regulations because proposed section 2591.1 expressly provides that the regulations are inapplicable to the extent they conflict with the provisions of any statute or other regulation that more specifically addresses a particular violation.</p>
	2591.3(c)	<p><i>Section 2591.3(c) - Willfulness</i></p> <p>Several penalty provisions in the Insurance Code make a distinction between willfulness and knowledge (e.g. Insurance Code Sections 790.035 and 1858.07). The distinction is important because much</p>	<p>Any inconsistencies with existing law are resolved by the following language in Section 2591.1 of the proposed regulations: “To the extent that the provisions of this article conflict with the provisions of any statute or other regulation that more specifically addresses a particular violation, this article shall be inapplicable.”</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>distinction is important because much higher penalties are assigned to willful acts.</p> <p>Willfulness and knowledge are different concepts. Willfulness includes not only knowledge of a violation but also the “specific intent to commit such violation” (Insurance Code Section 1850.5). The proposed regulations blur the distinction between willful and knowingly. The regulations provide that violations may be considered willful when an insurer promulgates procedures not in compliance with the law, when an insurer fails to adopt reasonable standards or when an insurer fails to take remedial action even though these actions are not taken with the specific intent to commit a violation. The closing paragraph of subsection (c) of Section 2 states that willfulness is to be attributed to an insurer unless the insurer’s employee takes an action “not in the interest of the insurer.” This broad, nebulous standard is inconsistent with the specific intent that is required to</p>	<p>It is useful to note that the proposed regulations come into play only when an insurer has violated the law. Further, the regulations are not “intended to be consulted by a hearing officer, judge or trier of fact” (Section 2591.1(d) of the amended text) but instead are “appropriate for determining the penalty imposed in those cases that are resolved through settlement” (Section 2591.1(a) of the amended text). The regulations do not change existing legal definitions of knowledge, specific intent or willfulness, or blur the legal distinctions among these concepts. The regulations merely indicate that, given there has already been a violation of the law, no such distinction will be made in the Department’s deliberations as to whether or not to take an enforcement action and as to the penalty amount.</p> <p>The language to which the commenter objects (“not in the interest of the insurer”) has been deleted in the Amended Text of Regulation.</p> <p>Existing law is utterly silent as to how, at the prehearing stage, the Department is to arrive at an exact amount from within the applicable range of penalty amounts spelled out in each of the penalty provisions of the statutes the proposed regulations are implementing; there can therefore be no inconsistency in this regard. Further, there is no basis in law for the commenter’s apparent belief that insurers that violate the Insurance Code are not liable for each violation. Moreover, the proposed regulations do nothing in the way of changing what constitutes a willful violation. Nothing in the proposed regulations renders unlawful currently lawful conduct. Further, if a violation does not meet the pertinent existing legal standard for what constitutes a willful violation, then the statutory penalty provision addressing such a willful violation will not come into play, and the “high level of</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>show willfulness.</p> <p>The heavy penalties which the regulations would impose under the regulations' arbitrary "willful" standard are especially alarming because the regulations require the commissioner to "impose a penalty for each act." Under the regulations' description of willfulness, a negligent action by an insurer that is repeated numerous times would result in a huge penalty because of the high level of penalties associated with willful violations.</p> <p>Moreover, the regulations seem to attempt to establish a standard for willfulness that could conceivably render even lawful conduct unlawful. For example, an insurer may "promulgate procedures" that it believes to be in compliance with the law, but that the Department subsequently determines, based on its interpretation of the law, to be out of compliance. Under the proposed regulations, the insurer's conduct could be considered willful, even</p>	<p>penalties" of which the commenter speaks will not be applicable. Only penalties currently authorized by the Insurance Code and the regulations promulgated thereunder will be assessed. The proposed regulations do not change this fact, despite the commenter's assertions to the contrary.</p> <p>The language of the regulations is clear. The proposed regulations therefore do not run afoul of the Administrative Procedure Act's clarity standard. Specifically, the "but not limited to" language identified by the commenter does not represent a clarity problem. The proposed regulations' definition of knowledge/willfulness is necessarily broad, in order to encompass a wide range of factual circumstances, not all of which can reasonably be anticipated at the present time. It would be impracticable to attempt to list in the proposed regulations every possible example of illegal behavior on the part of insurers that, following the determination that a particular statute has indeed been violated, the Department will consider willful or knowing in its decisions as to whether or not to pursue and enforcement action and as to the penalty amount to be sought.</p> <p>Insurers are in fact already on notice as to the type of conduct that existing law identifies as willful. Insurers will continue be charged with a degree of knowledge of the law sufficient to avoid violations of the Insurance Code, in the same way they currently are. The proposed regulations in no way alter what constitutes a violation. Furthermore, once a violation has taken place, the proposed regulations puts insurers on notice that, when willfulness is an element of the particular violation they have committed, the Department, in its decision with regard to penalty amount, will utilize the broad standard of willfulness outlined in the regulations. In other words, the regulations will in no</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(d)	<p>though it promulgated the procedures based on its good faith understanding of legal requirements. Such a standard would not meet the Government Code’s clarity requirement and would result in unfair and unauthorized penalties against the insurer.</p> <p>Finally, the inclusion of the phrase “but are not limited to” in section 2591.3 (c) implies that the Department may consider violations willfully or knowingly committed based on an unknown standard not set forth in this section. The inclusion of the phrase renders the provision vague and results in a lack of notice as to the type of conduct that will in fact be considered willful and thus deserving of a higher penalty.</p> <p><i>Section 2591.3(d) – Monetary Effect</i></p> <p>This criterion needs further clarification. It should be made clear that this criterion is not to be administered in a manner which allows the commissioner to impose</p>	<p>outlined in the regulations. In other words, the regulations will in no instance operate to mitigate a penalty amount on the basis that a violation which satisfies the existing legal standard for willfulness is somehow less willful than any other violation of the same statute or regulation.</p> <p>The regulations reflect a choice by the Department that the exact nature or extent of guilty knowledge on the part of violators will not ordinarily be considered in the Department’s decision making process, once it has already been established that a particular statute has been violated. Instead, the affirmative existence of facts satisfying the criteria listed in Section 2593.1 will form the basis of the Department’s determinations as to which violations will be pursued by enforcement actions. The legal distinctions between knowledge and willfulness will of course continue to be observed, both by the Department and by the courts, with regard to the determination of whether or not there has in fact been a violation in the first place and with regard to the determination of whether the violation was or was not willful for purposes of applying the appropriate statutory penalty provision.</p> <p>The commissioner has considered this comment and rejects it. To the extent that this comment suggests that a penalty amount will be assessed solely based upon a company’s financial condition, the comment is incorrect. It is not the insurer’s financial condition that is considered under this criterion. Rather, the regulation text is clear that it is the</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(h)	<p>heavy penalties on a company simply because the company is in a good financial condition. Insurance Code Section 1292.1(a)(7) does not authorize the use of “financial impact” as a guideline. The statute provides that the guidelines are to be based on the nature, severity and frequency of the insurer’s violations. The statute makes no mention of the consideration of an insurer’s financial condition.</p> <p><i>Section 2591.3(h) - Previous Actions</i></p> <p>It is difficult for insurers to judge the fairness of enforcement or penalty decisions based on previous actions because we lack complete data on previous actions that may have been taken. Moreover, subsection (h) seems to say little. The first two sentences indicate that the commissioner may consider previous actions. The last sentence of the subsection states that the commissioner may totally disregard previous actions when deciding to undertake an enforcement action or in</p>	<p>financial impact of the violation upon the insurer that is taken into consideration and no further clarification is necessary. The regulation specifically states “gain” or “loss” which are terms that have nothing to do with the insurer’s financial condition. The gain or loss experienced by the insurer is indicative of the severity of the violation. As the impact of the violation is clearly part of severity, and severity is a specifically authorized criterion pursuant to CIC section 12921.1(a)(7), monetary effect can be considered.</p> <p>The Commissioner has considered this comment and rejects it. The purpose of the proposed regulation is to provide the Department with criteria to pursue enforcement actions and penalties consistently, fairly and equitably. To that end, the proposed regulation provides that the commissioner may take into account previous actions against insurers of similar size and circumstance. The commenter quotes accurately from the language of Section 2591.3(h), but then draws a conclusion not based on the quoted language. The language does not “say little” but rather provides the Commissioner with flexibility as well as meeting the goal of consistency.</p> <p>For the purposes of these regulations, it is not necessary for an insurer to judge the “fairness” of prior enforcement and penalty actions. It is not the intent of the proposed regulations, or the statutes they implement, to give would-be violators advice in advance as to which of their violations will or will not be pursued through enforcement actions or receive stiff</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	Notice of Proposed Action	<p>setting higher penalties.</p> <p><i>Mitigation</i></p> <p>The proposed regulations fail to adequately take into account mitigating circumstances. ACIC believes that mitigating circumstances must be part of any set of guidelines for enforcement or penalties.</p> <p><u>Notice of Hearing</u></p> <p>There are four statements in the</p>	<p>penalties. That is, the regulations are not intended to provide insurers with a means of determining when it will be to their benefit to violate the law. Insurers are to avoid all violations of the Insurance Code.</p> <p>The proposed regulations, contrary to the commenter's assertions, adequately take into account mitigating circumstances. Section 2591.3, subdivision (h) (Extraordinary circumstances) is a mitigating factor. In addition, Paragraph 2591.3(b)(2) (according to the paragraph numbering in the Amended Text of Regulation) indicates that in assessing the severity of a violation, consideration may be given to the necessary complexity of the transaction — another mitigating factor. Still another mitigating factor, the insurer's efforts to provide restitution and correct the non-compliant activity, appears in paragraph (f)(2) of the amended text of Section 2591.3. Moreover, language has been added to the Amended Text of Regulation (Section 2591.4, subdivision (a)) to the effect that inapplicability of one or more criteria will not have a mitigating effect. The Department will not, for example, consider lack of willfulness as a mitigating factor with regard to a violation that does not require willfulness in the first place. Ascribing significance to the absence of facts indicating the existence of an inapplicable criterion, as in this example, would amount to an illegitimate double discount on the penalty for unlawful behavior.</p> <p>1) The Commissioner has considered the comment and acknowledges that the quoted language was erroneously posted in the Notice of Hearing. The Notice of Hearing was drafted while the</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	and Public Hearing	<p>Department of Insurance’s notice of hearing on the proposed regulations which should be clarified.</p> <p>First, the Policy Statement Overview’s description of the criteria in the proposed regulations includes “the degree to which a penalty or enforcement action may deter future violations.” This criterion does not appear in the regulation’s list of criteria.</p> <p>Second, the Policy Statement Overview includes the statement that “the regulations provide examples of how these criteria would be applied to hypothetical violations.” Hypothetical violations are not included in the proposed regulations.</p> <p>Third, the notice’s discussion of economic impact states, “The Department has made an initial determination that the adoption of this regulation may have a significant statewide adverse economic impact on businesses, including the ability of California businesses to compete with</p>	<p>Department was still deciding upon the language of the initial proposed regulation text. The language quoted in the comment reflects a provision that the Department ultimately decided to remove from the proposed regulation before the Department filed its Notice of Proposed Action. Due to sheer oversight, the Department neglected to omit the corresponding description of this deleted language in the Notice of Hearing. However, as is noted in the comment, the regulations do not include a provision for “the degree to which a penalty or enforcement action may deter future violations.” Because the proposed regulation text never has, and never will contain a provision for the quoted language, no further action is necessary.</p> <p>2) The Commissioner has considered the comment and acknowledges that the quoted language was erroneously posted in the Notice of Hearing. The Notice of Hearing was drafted while the Department was still deciding upon the language of the initial proposed regulation text. The language quoted in the comment reflects a provision that the Department ultimately decided to remove from the proposed regulation before the Department filed its Notice of Proposed Action. Due to sheer oversight, the Department neglected to omit the corresponding description of this deleted language in the Notice of Hearing. However, as is noted in the comment, the regulations do not include “examples of how these criteria would be applied to hypothetical violations.” Because the proposed regulation text never contained a provision for the quoted language, no further action is necessary.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>businesses in other states.” This statement indicates a belief that the adoption of the criteria in the proposed regulations will significantly increase the penalties imposed on insurers doing business in California. If this is the Department’s purpose in promulgating the proposed regulations, insurers and the public should be provided with the specifics of this change in regulatory practice.</p> <p>Fourth, the notice of hearing describes the proposed regulations as “guidelines” however, the regulations are also described as “prescriptive standards.” This creates some confusion regarding whether the Department will use the regulations’ criteria as flexible guidelines or mandated, strict standards. Some clarification on this point is needed.</p> <p>The insurance commissioner has broad authority to enforce California insurance laws and to regulate California’s insurance market. <i>(California Insurance Law and</i></p>	<p>3) The Department does not intend for these regulations to increase the penalties imposed on insurers doing business in California. Rather, these regulations are designed to provide more formal structure in the decision making process. Specifically, these regulations are designed to help the Commissioner determine whether to initiate an enforcement action and to determine the appropriate penalty from the range of penalties available. Thus, because the proposed regulations concern when and how much penalty will be assessed, the Department has concluded that these regulations may have a significant impact directly affecting business. Pursuant to Government Code section 11346.5(a)(7), therefore, the Department has notified the public of this possibility.</p> <p>4) According to Webster’s II New Riverside Dictionary, a “guideline” is “a statement or outline of procedure or policy.” Guidelines, by definition, may be either prescriptive or performance driven in nature. The guidelines listed in the proposed regulations represent prescriptive standards, because they require the Commissioner to take every factor under consideration in deciding whether to conduct an enforcement action and assess penalties. Thus, as was stated in the Notice of Proposed Action, these proposed regulations impose prescriptive standards upon the Department. The comment questions whether the guidelines will be flexible or mandated. In short, the guidelines provide strict standards regarding what criteria the Commissioner must consider in deciding whether to initiate an enforcement action and weighing appropriate penalty. The guidelines are flexible, insofar as the Commissioner may decide the</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p><i>Practice, §1.07</i>) The insurance commissioner is more than a policeman. The commissioner is responsible for maintaining a healthy insurance market in California. Existing law gives the commissioner the discretion and flexibility to enforce insurance laws in a manner that balances the interests of consumer protection, fairness and the goal of maintaining a competitive, sound insurance market. The criteria listed in the proposed regulations should not be administered in a manner that deprives the commissioner of discretion and flexibility. The regulations must not straightjacket the commissioner into formula-type prescriptive standards that would force enforcement actions and impose penalties when enforcement and penalties may not be in the best interests of long-term regulatory goals and a healthy California insurance market.</p> <p>The proposed regulations must not undermine the public policy in favor of settling disputed violations.</p>	<p>relevance of each guideline, as applied to the facts of each individual case. Therefore, the Commissioner agrees with the comment, to the extent that it notes that “the proposed regulations should not be administered in a manner that deprives the commissioner of discretion and flexibility.” Indeed, when conducting enforcement actions and attempting to settle such cases, the Commissioner is cognizant of the importance in resolving each matter in a fair and equitable manner. Flexibility is crucial to equitable enforcement. The Commissioner is confident that the proposed regulations strike the appropriate balance between flexibility and structure necessary for the enforcement of the Insurance Code.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>Regulatory settlements allow the Department to direct insurer actions that remediate problems and assure compliance with laws and regulations. We are concerned that if the regulations are administered in a manner that presents insurers with huge potential penalties, many insurers will be forced to take cases to administrative hearing or judicial decision. This would subvert good regulatory policy.</p> <p>ACIC appreciates the Department of Insurance's consideration of these comments. We trust that our comments will help the Department to improve the proposed regulations.</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
<p>Doug Heller On behalf of the Proposition 103 Enforcement Project, a project of the Foundation for Taxpayer and Consumer Rights</p> <p>December 17th, 2002 Written submission via e-mail.</p>		<p>The Proposition 103 Enforcement Project (The Project)¹ submits the following comments in response to the California Department of Insurance's (CDI) revised Regulations for Enforcement Actions and Penalties.</p> <p>The revised regulations address some of the specific problems identified in the initial draft regulations. However, the Project continues to oppose certain aspects of the regulations and urges the Department to address these issues. We maintain our opposition to the regulations insofar as the rules would provide regulatory loopholes that may be used to limit the scope of enforcement actions by the Commissioner.</p> <p>Because the Department failed to address certain important concerns</p>	

¹ The Project was formed in 1993 and is a project of the Foundation for Taxpayer and Consumer Rights (FTCR"), a 501(c)(3) non-profit, non-partisan public benefit corporation organized to represent the interests of consumers. The Project is dedicated exclusively to the protection of the interests of all insurance consumers in matters concerning Proposition 103 (the 1988 voter-enacted insurance reform initiative) before the Legislature, the CDI, and the courts. The Project acts to defend, enforce and implement the provisions of the initiative and other consumer protection measures enacted for the benefit of consumers and policyholders.

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>address certain important concerns addressed in our previous comments, we have reiterated the relevant comments in this letter.²</p> <p><u>I. STRONGER ENFORCEMENT IS NEEDED</u></p> <p>There is no question that one of the key areas where the CDI's regulation of the insurance industry needs to improve is in the enforcement of the Insurance Code and the punishment of wrongdoers.³</p> <p>As we noted in our previous comments, a vast majority of known</p>	<p>I - The Commissioner has considered the comment and rejects it. The Department conducts a wide range of activities designed to bring insurers into compliance with the many requirements of the Insurance Code. Aside from those instances where a penalty is mandated by statute for a given offense, it is neither feasible nor prudent to impose penalties upon every observed violation, no matter what the underlying circumstances reveal. The Legislature expresses a penalty provision in mandatory terms, when it intends for a state agency to impose a penalty without discretion. The logical corollary to this rule is that those penalties, which are not mandatory may be imposed at the discretion of the Department.</p>

² The Project's initial comments were submitted to the Department on October 2, 2002.

³ Unless otherwise indicated, all information in this section regarding CDI enforcement actions is taken from its website, <http://www.insurance.ca.gov>.

⁴ For other examples of Insurance Code provisions that contain mandatory or directive language, or otherwise limit the commissioner's discretion to not seek penalties for known violations (such as by setting a minimum penalty for violations), see §§ 789.3 1858.1, 1858.3, 1858.07, 1861.14, 10140.1, 10234.3, 10509.9, and 12414.25.

⁵ For other examples of penalty schemes that provide for reduced penalties for violations that are either not "willful" or not "knowing," see §§ 789.3, 790.035, 790.07, 10140.1, 10140.5, 10149.1, 10509.9, 11756, and 12414.25.

⁶ For other examples of penalty schemes that provide for reduced penalties for first-time violations, see §§ 790.07 and 10509.9.

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>violations of the Insurance Code go unprosecuted and unpunished by the Department and thousands of insurer violations identified by the Department through market conduct examinations and other administrative proceedings have gone unpunished. The following is a recent example:</p> <p>On March 6, 2002, the CDI released its market conduct examination report for Coast National Insurance. The review of 391 closed claims files uncovered 184 violations, including violations of Insurance Code 790.03 for failure to adhere to standard of prompt investigation and processing of claim and numerous other violations of California code and regulation. The MCE indicates that \$1005.26 was recovered as result of the exam but there is no indication that any fine or penalty was imposed on the company.</p> <p>With only seven enforcement actions</p>	<p>The Department routinely takes steps to force insurers into compliance with the Insurance Code using methods that do not necessarily result in a formal enforcement action. For example, when the circumstances surrounding a market conduct examination suggest that a company is prepared to make amends for potentially inappropriate or illegal rating and underwriting, the Department has the discretion to expedite the return of premium for consumers, rather than engage in a costly and time-consuming enforcement action.</p> <p>For that matter, in those cases that do require enforcement proceedings, one critical component of any enforcement action is the option of settlement. Settlements, by their very nature, represent a compromise between the parties. Settlement may be the most prudent option when, for example, a statute that is the basis for a violation is reasonably susceptible to more than one meaning. Similarly, the circumstances of a particular insurer or its policyholders may require that the insurer pay penalties of a lesser or greater amount than typically imposed. It is the position of the Department that judgment and equity must enter into any decision to conduct an enforcement action or assign an appropriate penalty. The proposed regulations provide instructions to the Department and the public, which will promote the equitable and consistent enforcement of the Insurance Code.</p> <p>The effect of these regulations cannot be measured without application in practice. The proposed regulations are not intended to limit the number of times the Commissioner initiates enforcement actions or imposes penalties. For that matter, it is the Department's belief that the proposed regulations will facilitate the ability of the Department to</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>taken against insurers by the Department in 2001, it is clear that the CDI initiates enforcement actions too infrequently and settles for too little, in many cases failing to enforce the expressly mandated penalties in the Insurance Code.</p> <p>The Project is encouraged by the Department's effort to establish guidelines for imposing penalties, and we hope that clearer standards for assessing penalties will lead to more and consistent enforcement of the Insurance Code. However, we remain concerned that the regulations might be used to avoid pursuing enforcement actions against insurers. There should be a presumption at the agency that any violation of the Insurance Code for which the Insurance Code provides penalties should result in a fine or other enforcement action. Strictly applying the penalties specified in the Insurance Code for violations should be the general rule – not the exception.</p>	<p>conduct enforcement actions in the future.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.1	<p><u>II. CRITERIA SHOULD NOT BE USED TO DETERMINE WHETHER OR NOT TO TAKE AN ACTION WHEN PENALTIES ARE MANDATED BY LAW</u></p> <p>The regulations provide guidelines for both the determination of whether an enforcement action should be taken and the amount of penalty to be imposed. The revised regulations state that these rules are “inapplicable” if the rules conflict with existing law that “more specifically addresses a particular violation.” [Section 2591.1] Nevertheless, the statutes referenced for this section include sections of the Insurance Code that have mandatory penalties. For example, section 11756 of the Insurance Code provides in part:</p> <p style="padding-left: 40px;">Failure to comply with commissioner's final order. Any person, insurer, or organization, who fails to comply with a final order of the commissioner under this</p>	<p>II – The Commissioner has considered the comment and rejects it. The commenter correctly points out that some of the statutes referenced for this regulation include provisions of the Insurance Code that require a range of mandatory penalties, under some circumstances. The commenter also states that these “criteria should not be used to determine whether or not to take an action when penalties are mandated by law.” The proposed regulations, however, acknowledge that the Commissioner shall not use the criteria to determine whether a particular violation warrants an enforcement action when existing law requires a penalty from within a range for specified conduct. Indeed, as the commenter notes, this article is inapplicable, to the extent that its provisions conflict with any statute or other regulation that more specifically addresses a particular violation. It is important to note that the proposed regulations are designed to decide two independent questions: 1) whether or not a violation warrants an enforcement action and 2) what amount of penalty should be imposed from within a range of penalties. In the examples provided by the commenter, the proposed regulations will apply to the second question, but will not apply to the first.</p> <p>Thus, in the examples provided by the commenter, concerning Insurance Code sections 11756 and 1859.1, the proposed regulations do not apply to the question of whether a violation of sections 11756 or 1869.1 warrants an enforcement action, because the statutes in question expressly require an enforcement action. With regard to the question of the appropriate penalty amount, however, the statutes do not specify an appropriate amount. Rather, the statutes provide penalty</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>article shall be liable to the state in an amount not exceeding fifty dollars (\$50), but if the failure is willful, he, she, or it shall be liable to the state in an amount not exceeding five thousand dollars (\$5,000) for the failure. <i>The commissioner shall collect the amount so payable</i> and may bring an action in the name of the people of the state of California to enforce collection. These penalties may be in addition to any other penalties provided by law. (emphasis added)</p> <p>And section 1859.1 provides in part:</p> <p>Any person, insurer, organization, group, or association who fails to comply with a final order of the commissioner under this chapter shall be liable to the state in an amount not exceeding fifty thousand</p>	<p>ranges, which depend in part upon whether the violation is willful or non-willful. Because these statutes do not provide guidelines for determining a penalty from within the specified range, these regulations will be used to determine the appropriate penalty amount.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>dollars (\$50,000) but if the failure is willful he or she or it shall be liable to the state in an amount not exceeding two hundred fifty thousand dollars (\$250,000) for the failure. That penalty shall be in addition to any penalty arising under Section 1858.07. The commissioner <i>shall collect</i> the amount so payable and may bring an action in the name of the people of the State of California to enforce collection. (emphasis added)⁴</p> <p><u>The regulations should explicitly state that the Commissioner shall not use the enumerated criteria to determine whether a particular violation warrants enforcement action, when existing law mandates a penalty and leaves the Commissioner with no discretion as to whether or not an action is taken.</u></p> <p><u>III. REGULATIONS SHOULD PROMOTE ACTION AGAINST ALL VIOLATIONS OF LAW</u></p>	<p>III. To the extent that this comment suggests that an enforcement action should be taken every time the Department observes a violation of the Insurance Code, see the first comment in response to section I,</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>In addition to the concern expressed in Section II, above, the proposed regulations provide the Commissioner far too much discretion with respect to whether or not an enforcement action should be taken when the Insurance Code does not specifically delineate action and penalties. Irrespective of the existence of an explicit statutory penalty, there should still be a presumption that each and every violation will be addressed. Otherwise, insurers will be invited to assess when a violation is not really a violation by virtue of lax or no enforcement.</p> <p>The regulations, and the implementation of the rules, should ensure that regulated entities are convinced that they will be subject to enforcement actions whenever they violate the law. At a minimum, the regulations should require the Commissioner to justify in writing any failure to take formal enforcement action with respect to known violations.</p>	<p>above.</p> <p>To the extent that this comment suggests that the proposed regulations will not address some violations, thereby inviting insurers to violate certain provisions of law, the Commissioner has considered the comment and rejects it. The Commissioner is required to perform all duties imposed upon him and enforce the execution of those provisions of the Insurance Code and other laws regulating insurance. (Ins. Code § 12921(a).) To that end, the proposed regulations will ensure that a consistent methodology is used to enforce those provisions of the Insurance Code that authorize enforcement and penalties. To the extent that the Legislature has not given the Commissioner the power to impose penalties for certain violations, the Department cannot create such a duty through regulation. (Govt. Code § 11145.) The Commissioner intends for these regulations to promote consistent enforcement and penalties for those provisions of law that give the Commissioner the power to conduct enforcement actions and impose penalties. Anything more would exceed the Department’s authority. If the regulations required the Commissioner to justify in writing any failure to take formal enforcement action for known violations, this would result in notice that a particular violation will not be pursued, which is exactly the kind of notice that this comment seeks to avoid. In other words, there are provisions of the Insurance Code, which do not provide the Commissioner with the authority to impose a penalty or conduct an enforcement action. If the Commissioner were to make each of those provisions known to insurers, “insurers will be invited to assess when a violation is not really a violation by virtue of lax or no enforcement.”</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(c)	<p><u>IV. THE REVISED REGULATIONS WOULD ALLOW INSURERS TO ESCAPE ACCOUNTABILITY</u></p> <p>Section 2591.3 (c) provides, in the last paragraph: In the case of an employee or agent or contract entity conducting business on the insurer’s behalf, willfulness shall be attributed to the insurer unless the employee, agent or contract entity has acted outside of the scope of employment or <i>otherwise not in the interest of the insurer at the time the act is committed.</i> (emphasis added)</p> <p>In this subsection, the phrase “or otherwise not in the interest of the insurer” should be stricken, because only without this phrase will the provision hold insurers accountable. Assuming that penalties are appropriately high, <i>any</i> action by an employee that is discovered by the</p>	<p>The language Mr. Heller objects to has been stricken from the Amended Text of regulation, in response to this comment.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(c) and 2591.3(e) (5)	<p>CDI and determined to be a violation of the Insurance Code will be an action “not in the interest of the insurer.” The final phrase would be used by insurers to escape liability, and is unnecessary in any case, as the phrase providing immunity for acts committed by employees acting “outside the scope of employment” provides sufficient protection to insurers.</p> <p><u>V. THE REGULATIONS WOULD PROVIDE MANY VIOLATORS WITH AN UNWARRANTED DOUBLE DISCOUNT</u></p> <p>Sections 2591.3 (c) and 2591.3 (e)(5) provide that the Commissioner may reduce penalties when violations are not knowing or willful, and when a previous related action has not been taken against the insurer. However, in many cases the maximum available penalty will <i>already</i> reflect whether or not the violation was willful or knowing, and whether or not the violation was a first offense. Thus,</p>	<p>V - In response to this comment language has been added to the Amended Text of Regulation (Section 2591.4, subdivision (a)) to the effect that inapplicability of one or more criteria will not have a mitigating effect. The Department will not, for example, consider lack of willfulness as a mitigating factor with regard to a violation that does not require willfulness in the first place. Ascribing significance to the absence of facts indicating the existence of an inapplicable criterion, as in this example, would indeed amount to an illegitimate double discount on the penalty for unlawful behavior. Our added language addresses this and similar concerns.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>applying the criteria specified in these sections to determine the amount of penalties would result in an unwarranted “double discount” for wrongdoers.</p> <p>For example, section 1858.07 of the Insurance Code provides for a fine of \$10,000 for certain “willful” violations of the rate laws. However, the maximum fine for similar violations that are not willful is set at \$5,000, or fifty-percent less than the maximum available fine for willful violations.⁵ Thus, non-willful violators are <i>already</i> liable for reduced penalties as a result of their less culpable mental state.</p> <p>Similarly, Insurance Code subsection 10140.5(b) provides penalties for certain unlawful discriminatory practices of up to \$2,500 for first-time violations by insurers, but up to \$5,000 for subsequent violations.⁶ Thus, again, one of the criteria that would be used under these proposed regulations to reduce penalties has already been factored into the</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(f)	<p>maximum available penalty.</p> <p><u>The regulations should clarify that subsections (c) and (e)(5) shall not be considered if the law already accounts for whether or not a violation was knowing, willful and/or a first time offense.</u></p> <p><u>VI. “DURATION OF THE NON-COMPLIANT ACTIVITY” CRITERION MISSTATES THE LAW</u></p> <p>Section 2591.3 (f) is both confusing and legally incorrect: The duration of the non-compliant activity. For the purposes of this criterion, consideration will be given as to whether the violation was a single event or continued repeatedly over a given period of time.</p> <p>Violations repeated “over a period of time” constitute a series of separate violations, each punishable by a separate penalty. It is important to</p>	<p>VI - The commissioner has considered this comment and a change to the regulation text was made. “Violation” was changed to “violations” in order to make clear that even if the violations are ongoing, they will be identified as more than one violation. Although the language in this subsection goes only to one criterion used in determining duration for purposes of whether to bring an enforcement action and the appropriate penalty and in no way provides that multiple violations will be treated as one single violation, the change was made for clarity. To the extent that the proposed language was misinterpreted and in order to avoid any confusion, the text was changed.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.1	<p>note that while violations that are repeated or are part of a general business practice may be punishable by enhanced penalties, these enhanced penalties apply to each unlawful act. This subsection as written could easily mislead a CDI employee into treating a series of violations as a single infraction, and thus imposing only one penalty for the violations collectively.</p> <p><u>VII. REVISED REGULATIONS ADDRESS CERTAIN PROBLEMS IDENTIFIED BY THE PROJECT IN EARLIER COMMENTS</u></p> <p>Under the revised regulations, the penalty guidelines contained in the regulations can not be used to undermine more stringent penalties set forth in law, where the existing law “more specifically addresses a particular violation.” [Section 2591.1] This addresses our concern that the Commissioner would have too much discretion under the</p>	<p>VII - This comment approves of the proposed Section 2591.1, insofar as it states that the regulations are inapplicable when a provision of law “more specifically addresses a particular violation.” Therefore, no response is necessary to the comment, to the extent that it expresses approval for the language of Section 2591.1. However, to the extent that this comment restates its criticism as noted in commenter’s Section II, above, the Department incorporates by reference its response to Section II, above.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(b)	<p>regulations in instances in which the law provides for a mandatory penalty. This does not address our entire concern, however, as we indicate in Section II above.</p> <p>Section 2591.3 (b) provides the Commissioner with appropriate discretion in whether or not to consider the frequency of the occurrence of the violation and the number of people impacted by the violation. The earlier draft of regulations <i>required</i> the consideration of this section, which would be inappropriate with respect to certain violations. When violations are discovered through consumer complaints, for example, the CDI will often not have a statistically significant set of similar files on hand. This fact should not prevent the CDI from applying maximum penalties, if that is otherwise deemed appropriate.</p> <p>The revised regulations appropriately eliminated certain considerations in the determination of penalties,</p>	<p>To the extent that it is commented that the earlier draft of section 2591.3(b) required the consideration of this section, the Commissioner has considered this comment and respectfully rejects the comment as being incorrect. The original draft, as well as the final draft section 2591.3(eb), has always stated “In determining the frequency, consideration may (emphasis added) be given to the number of violations specifically identified and the number of persons reasonably determined to have been impacted over a given period of time by such violations within the insurer’s population of applicants, insureds, claimants, potential applicants or among its competitors and to the number of files in which the violation takes place compared to the number of files with a similar transaction but no violation.” The commenter urges that the Department should not be prevented from applying maximum penalties, if deemed appropriate, even in circumstances when violations are discovered through consumer complaints, and, for example, the Department doesn’t have a statistically significant set of similar files on hand. To address the commenter’s concerns, the language of the regulations is still applicable to one or a thousand files.</p> <p>This comment is not a criticism to the proposed regulation; therefore, no response is necessary.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>including the insurer's financial strength and the anticipated deterrent effect of an action. There should be no special consideration given to lawbreakers regardless of their financial circumstances, nor should a subjective assessment of the action's impact on others be considered in the application of penalties.</p> <p><u>VIII. THE CDI SHOULD IMPROVE THE PUBLIC'S ACCESS TO INFORMATION REGARDING THE CDI'S ENFORCEMENT ACTIVITIES</u></p> <p>In our previous letter, the Project urged the Department to include rules to improve the quality and amount of information available to the public regarding the agency's enforcement activities. The CDI should provide detailed information to enable the public to monitor the CDI's enforcement of the Insurance Code and identify trends in the CDI's enforcement over time. Ideally, this information should be broken down by insurer to ensure consistent</p>	<p>VIII - The Commissioner has considered the comment and has rejected it. The purpose of the proposed regulations is to implement enforcement actions and penalties consistently, fairly and equitably. An added benefit of these regulations is that they will provide a transparent view for the public to observe the criteria considered by the Department, when deciding whether to conduct an enforcement action or impose a penalty. The specific goal of the proposed regulations, however, is not to enhance or restrict the public's access to information concerning enforcement actions. To the extent that this comment suggests that more public access should be granted, the comment is not specifically directed at the proposed action or procedures followed by the Department in proposing or adopting the action.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>enforcement and to help the public easily identify compliant and noncompliant insurers. The information should be disseminated on the CDI's website and through monthly press releases to major California media outlets and interested members of the public who so request.</p> <p>Please refer to the Project's previous comments for our suggestions concerning data collection.</p> <p><u>VIII. CONCLUSION</u></p> <p>For the reasons stated above, the Project maintains its opposition to the CDI's Regulations for Enforcement Actions and Penalties. While we applaud certain improvements in the proposed regulations, we strongly encourage the agency to improve these revised regulations in order to address the remaining weaknesses.</p> <p>We appreciate this opportunity to comment on the Department's contemplated regulations, and would be happy to answer any</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		would be happy to answer any questions about our comments.	
Robert W. Hogeboom and Robert J. Cerny on behalf of Barger & Wolen, L.L.P. 515 S.		On November 1, 2002, the California Department of Insurance (“Department”) issued a Notice of proposed Action and Notice of Public Hearing with regard to contemplated Regulations for Enforcement Action and Penalties (the “Regulations”). The Regulations set forth guidelines and factors for the Department to consider in bringing enforcement actions and assessing penalties in	

⁷ A summary of the cited penalty provisions is attached as “Exhibit A.”

⁸ We note that “Authority” means the provision of law that permits the agency to adopt, amend, or repeal a regulation. Cal. Gov’t Code § 11349(b).

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
<p>Flower Street, 34th Floor Los Angeles, CA 90071 Written comments submitted via e-mail.</p>		<p>actions and assessing penalties in settlement negotiations. We respectfully request that the Commissioner reconsider the Regulations for the following reasons:</p> <p>(1) The Regulations should apply only to enforcement actions arising out of consumer complaints, as the governing authority at Insurance Code Section 12921.1 is limited to consumer complaints.</p> <p>(2) The Regulations are unnecessary as they establish mandatory guidelines that the Commissioner must follow in bringing enforcement actions and penalties, while at the same time they purport to allow the Commissioner total discretion in those same areas.</p> <p>(3) The Regulations broaden the scope of “willfulness” contrary to California law, which will</p>	

9 “Necessity” means that record of the rulemaking proceeding demonstrates by substantial evidence the need for the regulation to effectuate the purpose of the statute that the regulation implements, interprets or makes specific. Cal. Gov’t Code § 11349(a).

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591	<p>California law, which will increase the number and severity of enforcement actions and penalties.</p> <p>(4) The Regulations inappropriately attribute willfulness of an agent or employee to the insurer contrary to law.</p> <p>1. LEGAL AUTHORITY</p> <p><i>As the governing authority, Section 12921.1, is limited to enforcement actions arising out of consumer complaints, the Regulations should not apply to enforcement actions not arising out of complaints. The penalty statutes referenced in the Regulations, with one exception, do not authorize the Commissioner to promulgate penalty regulations. The exception is the Unfair Practices Act, which does provide such authority in Section 790.10. However, the Unfair Practices Act already has applicable penalty regulations, which would trump these Regulations.</i></p>	<p>The comment suggests that the Department lacks authority to make these regulations applicable to cases other than those that begin through the complaint investigation program described in Insurance Code section 12921.1. The Commissioner has considered the comment and rejects it. Subdivision (b) of proposed regulations section 2591 acknowledges that these regulations are intended to apply to more cases than simply those cases subject to Insurance Code section 12921.1(a)(7). Indeed, the Reference provision and section 2591.1 of the proposed regulations list the penalty provision statutes, which these regulations will implement, interpret and make specific. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department's authority to promulgate regulations which apply to other investigations of insurer conduct where the Department has inherent authority to implement its regulatory criteria.</p> <p>The penalty statutes listed in the Reference provision and section 2591.1 give the Commissioner authority to impose a penalty from within a range. For example, Insurance Code section 1858.07 authorizes the Commissioner to impose a penalty "not to exceed" \$5,000 for a non-willful violation and "not to exceed" \$10,000 if the violation is willful. Insurance Code section</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p><i>these Regulations.</i></p> <p>The Commissioner proposes the Regulations under the authority of Section 12921.1 of the California Insurance Code (“Code”), which <i>requires</i> the Commissioner to establish a program to investigate and respond to consumer complaints and to bring enforcement actions against insurers when warranted. Section 12921.1(a)(7) mandates that the program include a list of criteria to determine which violations should be pursued and enforcement guidelines for the determination of penalties for violations based on the nature, severity and frequency of the violations. These Regulations, therefore, fulfill the Department’s obligation to promulgate enforcement guidelines for complaints under Section 12921.1(a)(7).</p> <p>While the Regulations are certainly authorized in connection with the investigation of complaints, the Preamble at Section 2691 greatly expands their scope:</p>	<p>12921, subdivision (a) requires the Commissioner to enforce the provisions of the Insurance Code and other laws relating to the business of insurance in this state. The Commissioner has inherent power to implement, interpret and make specific the manner in which these penalty ranges will be applied in practice.</p> <p><i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, “[The Commissioner’s] powers are not limited to those expressly conferred by statute; “rather, ‘[it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.’” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (Italics added.)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute.</p> <p>Here, the proposed regulations will apply to statutes which authorize the Commissioner to seek a penalty “not to exceed” a certain amount. (See, e.g., Ins. Code sections 1858.07 & 10140.5.) It is necessary to promulgate</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>“Pursuant to the Commissioner’s authority to enforce the Insurance Code, this article shall also apply to the findings generated by <i>other</i> enforcement activities that allege violations of the same statutes and regulations, <i>such as market conduct examinations or other Department investigations of insurer practices</i>. This article is intended to provide greater uniformity in enforcement and in the general assessment of penalties imposed on insurers.” (Emphasis added).</p> <p>As the Commissioner intends the Regulations to apply to many types of enforcement actions other than those arising from consumer complaints, the scope of the Regulations is too broad. The Regulations purport to apply to 19 different types of actions, whether or not the action arises from a consumer complaint.⁷ Of course, the authority of Section 12921.1</p>	<p>regulations for settlement purposes insofar as the statutes referenced in the proposed regulations authorize the Commissioner to impose penalties within a range, and therefore the Commissioner has inherent authority to create a regulatory scheme to decide appropriate penalties within that range. Furthermore, each agency has inherent (as well as statutory) power to settle cases prior to a hearing, in a manner in which the parties see fit. (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114.)</p> <p>Government Code section 11415.60 recognizes that “[a]n agency may formulate and issue a decision by settlement, pursuant to an agreement of the parties, without conducting an adjudicative proceeding. Subject to subdivision (c), the settlement may be on any terms the parties determine are appropriate.” Subdivision (c) states, in part, “The terms of a settlement may not be contrary to statute or regulation, except that the settlement may include sanctions the agency would otherwise lack power to impose.”</p> <p>Therefore, the Commissioner has broad discretion to adopt rules and regulations as necessary to promote the public welfare. The proposed regulations concern a number of statutes that give the Commissioner the power to impose penalties within a range after a hearing, but the statutes are silent regarding where the appropriate penalty is within the range. We also know that agencies are empowered to settle cases prior to hearing, and that the settlement may include sanctions which do not violate public policy that the agency would otherwise lack the power to impose. It is reasonable for the Commissioner to conclude that, when settling cases, he will use the statutory penalty ranges as a guideline for deciding what sanctions to impose at settlement. Moreover, the Commissioner’s broad discretion to adopt rules and regulations that “may fairly be implied from the statute granting the powers” authorizes him to</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>cannot extend to actions not arising from complaints. Yet the Department cites only one additional statute to support its authority – Section 790.10 – which authorizes the commissioner to promulgate regulations to administer the Unfair Practices Act, Section 790 <i>et seq.</i></p> <p>While we acknowledge that the Commissioner likely has authority to promulgate enforcement and penalty regulations for the Unfair Practices Act, it does not make sense to apply these Regulations to enforcement actions taken pursuant to that statute. The Department has recently proposed amendments to the Fair Claims Settlement Practices (“FCSP”) Regulations, which at Section 2695.12 contain factors that the Commissioner must consider in assessing penalties assessed for noncompliance with those regulations. <i>See</i> Cal. Ins. Code § 790.03(h)(listing the unfair claims settlement practices). Market conduct examinations under the authority of the Unfair Practices Act</p>	<p>fairly be implied from the statute granting the powers” authorizes him to create guidelines/criteria for enforcement and penalty assessment. (See, generally, <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825.)</p> <p>The authority to adopt these regulations may be fairly implied from those statutes that recognize the agency’s inherent power to settle cases “on any terms the parties determine are appropriate.” Additionally, the authority to adopt these regulations may be fairly implied from those statutes that designate a penalty range that may be imposed after a hearing.</p> <p>To the extent that this comment suggests the proposed regulations duplicate, or are inconsistent with the Fair Claims settlement practices regulations, the Commissioner has considered and rejects the comment. The comment does not cite any specific examples where there is an inconsistency between the proposed regulations and the Fair Claims settlement practices regulations.</p> <p>At least one commenter has argued that the proposed regulations do not meet the necessity standard, in light of the fair claims settlement practices regulations. This comment has been considered and is rejected. First, in the context of consumer complaints, the proposed regulations are necessary because Insurance Code section 12921.1(a)(7) expressly requires that we promulgate them.</p> <p>As the commenter notes, however, the Department has decided to promulgate these regulations for use in conducting enforcement actions that are initiated for reasons other than consumer complaints. Examples of the kinds of situations where the proposed regulations would also apply include enforcement actions, which are based upon the findings of</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>generally involve claims handling practices, and therefore the FCSP Regulations would apply. Accordingly, the Regulations at issue here would overlap and conflict with Section 12695.12. As Section 2695.12 is specific to claims examinations, it would override the Regulations in any case. Accordingly, the one penalty section, other than Section 12921.1, that provides the Commissioner with authority to promulgate the Regulations already has penalty regulations that would trump those at issue here.</p> <p>None of the other 18 cited penalty statutes authorizes the Commissioner to promulgate regulations setting guidelines for bringing enforcement actions or setting penalties thereon.⁸ Rather, the Legislature properly left these matters to the discretion of the commissioner holding office at the particular time. The Legislature did not intend that an insurance commissioner should promulgate regulations limiting the authority of</p>	<p>a market conduct examination or other Department investigation. Regardless of whether the Department conducts an enforcement action based upon the findings of a market conduct examination, a Department investigation, or in response to a consumer complaint, the decision regarding the appropriate penalty and whether to bring an enforcement action is the same. Therefore, the proposed regulations must cover more contexts than merely those cases where a consumer complaint has led to an enforcement action. If the proposed regulations did not apply to the findings from market conduct examinations or investigations, this would raise a potential consistency problem. The regulations would be inconsistent because, by all accounts, enforcement actions and penalties are imposed in exactly the same way, regardless of whether they are initiated by a consumer complaint, the findings of a market conduct exam, or a Department investigation. Yet, by making the proposed regulations apply solely to consumer complaints, they could lead to inconsistent enforcement of actions, which arise under other circumstances. For the reasons mentioned above, the proposed regulations must necessarily apply to other situations where the Department discovers – through a market conduct exam, investigation, or other non-consumer-complaint context – that an enforcement action is needed.</p> <p>To the extent that this comment suggests the proposed regulations duplicate, or are inconsistent with the Fair Claims settlement practices regulations, the Commissioner has considered and rejects the comment. The comment does not cite any specific examples where there is an inconsistency between the proposed regulations and the Fair Claims settlement practices regulations, with the exception of California Code of Regulations, title 10, Section 2695.12. However, the proposed</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.4	<p>subsequent commissioners to bring actions or to settle them as they see fit.</p> <p>Therefore, the Commissioner only has authority to issue regulations that govern enforcement actions arising out of complaints and only in those cases in which the nature, severity and frequency of violations indicate that an action should be brought. The Commissioner must eliminate the above-quoted language in the Regulation applying it to those other enforcement actions and limit the scope of the Regulations to consumer complaints.</p> <p>2. THE REGULATIONS ARE UNNECESSARY</p> <p><i>The Regulations do not fundamentally change the present situation in which</i></p>	<p>regulations clearly indicate that they would be inapplicable under circumstances where the Fair Claims Settlement Practices regulations apply: the proposed regulations cannot be duplicative or inconsistent with the Fair Claims settlement practices regulations because proposed section 2591.1 expressly provides that the regulations are inapplicable to the extent they conflict with the provisions of any statute or other regulation that more specifically addresses a particular violation.</p> <p>The commenter suggests that the proposed regulations do not further the intent of the Legislature because they will force the hand of subsequent commissioners to bring actions or settle them as they see fit. This comment is misplaced, however. First, it is important to note that the proposed regulations are very flexible and are designed to preserve the Commissioner's flexibility in deciding which enforcement actions should be taken and how much penalty should be imposed. This is why proposed regulations Section 2591.4 allows the Commissioner to decide the relevance of each criterion and to apply unstated criteria, when circumstances warrant. Second, if and when any subsequent Commissioner decides that the proposed regulations are somehow limiting, that Commissioner is fully within his or her prerogative to repeal or amend these regulations in order to further the successor-Commissioner's goals.</p> <p>The APA's necessity standard is satisfied by Ins. Code §12921.1(a)(7), which mandates these regulations. Allowing the Department to consider relevant criteria and disregard criteria that, in the Department's judgement, are not relevant is not contradictory. Further, even if it were true that the regulations do not cause the Department to change its practice, there is simply no requirement that the regulations force the</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p><i>the Commissioner has discretion to consider or not consider any factor in negotiating settlements. However, because they will require the Department to justify settlements based on the various factors, they likely will impede such negotiations. Settlements are presently negotiated such that all relevant factors are considered due to the nature of an adversarial structure of the negotiation. There is no reason to believe that the Regulations will increase accountability or uniformity of settlements. Therefore, the Regulations do not meet the Government Code's standard of necessity.</i></p> <p>The Regulations apply various criteria that the Commissioner must consider in determining that an enforcement action should be pursued and in selecting the appropriate</p>	<p>Department to conduct its business any differently than at present. It would be sufficient for the regulations to codify that practice.</p> <p>Although the regulations do not purport to provide absolute predictability and consistency of outcomes, they do promote these worthy goals. Further, the regulations limit to a known universe the factors which are to be considered in determining whether to pursue an enforcement action, which is presently not the case. Even when an unlisted criterion is considered, Section 2591.4 explicitly requires such criterion to be stated during any settlement negotiations.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>and in selecting the appropriate amount of penalty. On the other hand, Section 2591.4 requires the Commissioner not only to determine which criteria are relevant and their appropriate weight, but also to take into consideration other criteria that do not appear in the Regulations. While the Commissioner must consider specified criteria, he may disregard those same criteria and add others if he sees fit. Given this contradiction, there is no need for the Regulations, at all.</p> <p>Section 2591.4 essentially reflects the present situation in which the Commissioner has total discretion to bring an enforcement action and determine the appropriate penalty. <i>See</i> Cal. Ins. Code § 12921 (empowering the Commissioner to enforce the provisions of the Code); <i>and</i> § 12924 (setting forth the Commissioner’s broad investigative authority). As the factors set forth in the Regulations are not mandatory, they would not provide the predictability and consistency of</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>outcomes that the Department claims they will. Therefore, the Regulations do not meet the Government Code's standard of necessity.⁹</p> <p>Based on our experience in handling numerous disciplinary matters over the past 25 years, the procedure followed by the Department in investigating and negotiating settlements with insurers has been relatively consistent. The only significant change in this area has been the amendment of Section 12921 requiring the Commissioner to review and approve every settlement and to disclose settlement stipulations on the Department website for public review. The Preamble states that the Regulations are intended to provide greater uniformity in enforcement and penalties. We have found, over time, that settlement negotiations with the Department take into account all of the relevant facts regarding the subject matter of each case, due to free negotiations between adversarial parties. Requiring the Department to disclose the factors considered would</p>	<p>This comment contends that if the Commissioner is forced to disclose the factors considered in conducting an enforcement action and assessing penalties, the effect will be to discourage settlements. The commenter goes on to cite <i>Fischer v. Superior Court</i>, 103 Cal.App.3d 434, 441 and <i>Rich Vision Centers, Inc. v. Board of Medical Examiners (1983) 144 Cal.App.3d 110, 114-16</i>, in support of the proposition that an agency has broad discretion to settle administrative cases on whatever terms and conditions that the parties believe are appropriate.</p> <p>The Commissioner agrees with the reasoning of those cases and the public policy that they represent. In fact, the Commissioner believes that the proposed guidelines will encourage, rather than hinder, settlement. It is also important to note that the proposed regulations are mandated by the Legislature, at least in part. (<i>See</i> Ins. Code § 12921.1(a)(7).) Because both the Department and the entity that is subject to enforcement will have access to the guidelines used by the Department, the parties will have more flexibility to negotiate an appropriate settlement within the construct of the guidelines provided in the regulations. The regulations will not bind future commissioners to a set of regulations that will impede negotiations with insurers, not only because the regulations are flexible, but also because future Commissioners will always have the prerogative to amend or repeal these regulations.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>hinder this process to the detriment of the Department and ultimately the public.</p> <p>This is contrary to the longstanding public policy to encourage settlements. <i>Fischer v. Superior Court</i>, 103 Cal. App. 3d 434, 441 (1980). In <i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i>, 144 Cal. App. 3d 110, 114-116 (1983), the court affirmed that administrative agencies and their attorneys have broad discretion to settle administrative cases. The principles expressed in the <i>Rich Vision</i> case were later reflected in Section 11415.60 of the Government Code, which provides that administrative agencies may settle cases on whatever terms the parties see fit. We further note that guidelines of this kind are extremely rare in the administrative arena, with virtually all states electing to retain commissioners' full discretion in settling cases. We are aware of no state in which an insurance department has had a positive experience with regulations</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2951.3(c)	<p>laying out guidelines required to be considered in bringing enforcement actions and setting penalties. It is our view that the Commissioner should consider carefully the potential ramifications of these guidelines before binding future commissioners to a set of regulations that will impede settlement negotiations with insurers.</p> <p>3. THE REGULATIONS IMPROPERLY EXPAND THE CONCEPT OF WILLFULNESS</p> <p><i>The Regulations improperly utilize the term “knowingly” as opposed to the proper term “willful.” Moreover, in stating the factors to determine willfulness, the Regulations are contrary to California case law interpreting that term. Insurers should be held to a willful standard only when the insurer has specific intent to commit the violation, as explained in</i></p>	<p>Any inconsistencies with the cited Insurance Code sections are resolved by the following language in Section 2591.1 of the proposed regulations: “To the extent that the provisions of this article conflict with the provisions of any statute or other regulation that more specifically addresses a particular violation, this article shall be inapplicable.”</p> <p>The proposed regulations in no way alter the definition of what constitutes willful conduct for purposes of determining whether a violation of the Insurance Code has taken place. Existing legal standards for willfulness, as specified in statute, regulation and case law are thus unaffected by, and are not inconsistent with, the proposed regulations.</p> <p>The commenter’s references to the willfulness standard in criminal and tort law is particularly inapposite in the context of insurance law. Furthermore, with regard to the citations to insurance case law, the identified analyses in each case address themselves to the question of</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p><i>case law. The factors as presently written violate the Government Code standard of consistency.</i></p> <p>Under Section 2591.3(c), the Commissioner must consider “the knowledge or willfulness of the noncompliant acts.” Further, subsections (c)(1) and (2) refer specifically to “knowledge.” Nonetheless, the level of penalty in many of the Code provisions cited by the Regulations depends on whether or not the act was “willful.” <i>See eg.</i> Cal. Ins. Code § 790.035. The term “knowing” is not used. Rather, “knowledge” is used only to determine whether or not a statute has been violated. <i>See</i> Cal. Ins. Code S. 790.03(h). Therefore, there is no basis to increase the penalty based on “knowledge” alone.</p> <p>Furthermore, the Regulations unduly expand the concept of willfulness itself. While there is no definition of willfulness in the Code, the factors for willfulness have been established</p>	<p>whether a statute has been violated. The proposed regulations, on the other hand, have no bearing on the question of whether a statute has been violated. The proposed regulations come into play only after it has been determined that an insurer has committed a violation of the law. The regulations do not change existing legal definitions of willfulness. The regulations merely indicate that, given there has already been a violation of the law, willfulness will be evaluated according to the language of the proposed regulations only in the Department’s deliberations as to whether or not to take an enforcement action and as to the penalty amount. Existing law is utterly silent as to how, given that a particular penalty provision is applicable, the Department is to arrive at an exact penalty amount from within the applicable statutory range of penalty amounts; there can therefore be no inconsistency in this regard.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>in case law. The factors listed in the Regulations, do not follow case authorities and therefore are inconsistent with California law.</p> <p>California courts have considered the term “willful” as used in a number of California statutes, as well as in tort and criminal cases, and the gloss on the term has varied depending on context. For example, a willful act in a criminal context involves some amount of malice; i.e., specific intent to do an act forbidden by law. <i>U.S. v. Drew</i>, 722 F.2d 551, 553 (9th Cir. 1983). In <i>Chow Bing Kew v. United States</i>, 248 F.2d 466 (9th Cir. 1957), a case involving an alleged violation of a statute prohibiting a person from “falsely and willfully” representing himself as a U.S. citizen, the court also emphasized the necessity that the prosecution prove the “specific intent” element when alleging the commission of a “willful” act under the statute. The court stated that to find “willfulness”, it must be proven beyond a reasonable doubt that the alleged violator <i>voluntarily and</i></p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p><i>deliberately</i> made the prohibited misrepresentation. <i>Chow Bing Kew, supra</i> at 469. Clearly, in the criminal context, an act must be more than merely accidental or inadvertent to be considered a willful act. Proving the specific intent to perform an act that is prohibited by law or to refuse to perform an act required by law is essential to proving the willfulness of an act.</p> <p>In civil cases, a quasi-criminal or “evil” intent is somewhat less prominent. However, the “specific intent” requirement for willfulness is every bit as necessary in civil cases as it is in criminal cases. In a workers’ compensation case, <i>Goodhew v. Industrial Accident Commission</i>, 157 Cal. App. 2d 252, 257 (1958), the court held that an employer “willfully” violated Labor Code Section 4554 as it “intentionally and deliberately failed to secure workers’ compensation coverage as to its corporate officers although it had knowledge that such coverage was required by law.” In holding Section</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>4554 had been violated, the court elaborated on the necessity of the presence of “specific intent” in acts it would consider to be “willful”:</p> <p style="padding-left: 40px;">In civil cases the word “willful” as ordinarily used in courts of law, does not necessarily imply anything blameable, or any malice or wrong toward the other party, or perverseness or moral delinquency, but [it does imply] that the thing done or omitted to be done, was done or omitted intentionally... That the person knows what he is doing, intends to do what he is doing, and is a free agent.”</p> <p style="padding-left: 40px;"><i>Id.</i></p> <p>In <i>Abron v. Workers’ Compensation Appeals Board</i>, 34 Cal. App. 3d 232, 237-238 (1973), the court held that</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>the mere failure to perform a statutory duty, in itself, is not willful misconduct. Rather, there must be actual knowledge of the penalty for failure to act coupled with the conscious failure to act to the end of averting injury. The employer must know the probable consequences of his failure to provide more adequate safety devices or a safer place to work and he must have put his mind to the existence of a danger to an employee and have failed to take precautions to avert that danger. <i>Abron, supra</i> at 238.</p> <p>In a case involving an alleged violation of an occupation safety standard by an electrical contractor the court in <i>Rick's Electric, Inc. v. California Occupational Safety and Health Appeals Board</i>, 80 Cal. App. 1023, 1034 (2000) utilized a similar interpretation of "willfulness" in the context of Section 334 of the Labor Code. The <i>Rick's Electric</i> noted that Section 334 establishes two different methods by which the willfulness of a violation could be established:</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>“(1) an employer <i>intentionally</i> violated a safety law; or (2) an employer had actual <i>knowledge</i> of an unsafe or hazardous condition, yet did not attempt to correct it.” (<i>Italics added</i>)</p> <p>The court held that under either of these tests, the appeals board must prove by a preponderance of the evidence that the employer committed a voluntary and volitional, as opposed to an inadvertent, act. The board was required to find that the act was the desired consequence of the actor’s intent and that the employer was conscious that this act violated a safety order. <i>Rick’s Electric, supra</i> at 1037.</p> <p>Based on the above, courts consistently hold that “willful” acts are not merely inadvertent or accidental. While civil cases de-emphasize malice, they have look for knowledge of the act, desire to</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(c)	<p>perform the act and awareness of its probable consequences. In <i>Rick's Electric</i>, the court also required consciousness that the act would violate the law. By including broad criteria for determining willfulness that are not contemplated in the case authorities, the Regulations violate the Government Code's standard of consistency, and will result in additional enforcement actions and unduly increase the severity of the penalties.</p> <p>4. THE REGULATIONS USE AN IMPROPER STANDARD OF AGENCY</p> <p><i>The Regulations automatically attribute willfulness of an employee or agent to the insurer. This is contrary to case authorities that require specific intent. It is especially inappropriate as insurers' employees and agents are often licensed themselves providing the</i></p>	<p>The proposed regulations do not come into play until there has in fact been a violation of California law, namely the Insurance Code, by an insurer. The fact that employees and agents may also be disciplined by the Department is of no consequence in the context of regulations setting out criteria for determining which violations by insurers the Department will pursue through enforcement action and what the exact penalty amount will be from among the range of penalty amounts set forth in the applicable penalty provision.</p> <p>Furthermore, principals who according to existing law have not committed a willful violation are not currently, and under the proposed regulations will not be, penalized for violating a statutory provision</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p><i>Department with jurisdiction directly over the employee or agent.</i></p> <p>At Section 2591.3(c), the Regulations provide that willfulness of an agent or employee generally will be attributed to the insurer:</p> <p style="padding-left: 40px;">“In the case of an employee or agent or contract entity conducting business on the insurer’s behalf, willfulness shall be attributed to the insurer unless the employee, agent, or contract entity has acted outside the scope of employment or otherwise not in the interest of the insurer at the time the act is committed.”</p> <p>As discussed in the previous section, California law does not automatically attribute willfulness to a principal or employer, and it is inappropriate to do so in these Regulations. We note that employees and agents are often individually licensed by the</p>	<p>requiring willfulness on account of the willful acts of their agents. Again, the proposed regulation only come into play once there has been a violation of the Insurance Code. Once there has been such a violation, however, the proposed regulations indicate only that willfulness on the part of an insurer’s agents will be ascribed to the insurer for the purposes of determining whether or not to pursue through enforcement action that violation and determining the exact penalty amount to be sought from within the applicable range. There is nothing in existing law to indicate that in the exercise of his discretion to make these two determinations, given that there has indeed been a violation of the Code, the commissioner cannot consider willfulness on the part of an insurer’s agents. And the commenter does not cite authority to the contrary.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>Department and therefore the Department would have a separate avenue to seek a penalty from that licensee. While the principal may be liable under respondeat superior for tort damages to a third party based on misconduct of an agent or employee, regulatory fines should only be sought against the licensee that committed the violation. What is more, principals should not be penalized for willfulness unless the principal actually commits an illegal act willfully – that is, unless it can be shown that the principal knew of the act and the violation of law. As drafted, subsection (c) is inconsistent with California law and should be revised to attribute willfulness to the insurer only if the insurer itself commits a wrongful act and knows its unlawfulness and probable consequences.</p> <p>5. CONCLUSION</p> <p>These Regulations are ill advised and illegal. They are illegal because they fail to meet the standards for</p>	<p>The commenter suggests that the proposed regulations do not further the intent of the Legislature because they will force the hand of subsequent commissioners to bring actions or settle them as they see fit. This comment</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>regulations in the Government Code. They are ill advised because they would unnecessarily constrain the ability of insurers and the Commissioner to make settlements because of the unreasonably high penalties that the Commissioner would be forced to seek and would substantially increase the number of enforcement actions that the Commissioner would be required to file. Under these regulations the working environment between the Department and the industry would become less efficient. Further, the risk of substantial fines for transactions not materially impacting the consumer may require a prudent business person to restrict or terminate participation in the California insurance market. Certainly, the Regulations may cause an insurer to hesitate to enter into or expand its presence in this state. At best, insurers will ignore the Regulations in settlement negotiations, rendering this regulatory action a waste of resources.</p>	<p>is misplaced, however. First, it is important to note that the proposed regulations are very flexible and are designed to preserve the Commissioner’s flexibility in deciding which enforcement actions should be taken and how much penalty should be imposed. This is why proposed regulations Section 2591.4 allows the Commissioner to decide the relevance of each criterion and to apply unstated criteria, when circumstances warrant. Second, if and when any subsequent Commissioner decides that the proposed regulations are somehow limiting, that Commissioner is fully within his or her prerogative to repeal or amend these regulations in order to further the successor-Commissioner’s goals.</p> <p>Moreover, the proposed regulations do not “force” a Commissioner to seek “unreasonably high” penalties. In fact, the regulations do not mandate any specific penalty amount. Rather, the regulations provide guidelines for enforcement and penalties. Thus, the Commissioner is not required to assess any particular penalty amount. Instead, the Commissioner is given the flexibility to look at each particular violation of law and determine whether an enforcement action is necessary and weigh the severity of the violation in assessing a penalty. It is this flexibility that will promote enforcement actions and penalties that are meted out in a fair and just fashion.</p> <p>The Commissioner rejects the comment that these regulations “may require a prudent business person to restrict or terminate participation in the California insurance market” and may “cause an insurer to hesitate to enter into or expand its presence in this state” because of the risk of substantial fines for transactions not materially affecting the consumer. Insurers are to avoid all violations of the insurance code. If a violation occurs, the commissioner may seek a penalty up to a certain amount.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>These regulations only help to determine where, within the applicable range, the penalty may fall. Whether a consumer is materially impacted by a violation is irrelevant to whether the violation occurred and whether the commissioner may levy a penalty. It is not the intent of the proposed regulations, or the statutes they implement, to give would-be violators advice in advance as to which of their violations will or will not be pursued through enforcement actions or receive stiff penalties. That is, the regulations are not intended to provide insurers with a means of determining when it will be to their benefit to violate the law. Violators are not to reap a windfall just because there happens not to be a showing of facts indicating a material effect upon consumers arising from their violations of the law.</p>
<p>Sherman A. Sitrin American International Companies State Regulatory Affairs General Counsel</p>		<p>Thank you for this opportunity to submit comments for your review and consideration in regard to the promulgation of the Regulations for Enforcement Actions and Penalties. We support the Insurance Department's efforts to develop these regulations and believe that providing the industry with the guidelines used by the</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
<p>175 Water Street, 18th Floor</p> <p>December 6th, 2002</p> <p>Written comments submitted via fax and mail.</p>	2591	<p>Insurance Department in settlement negotiations will help to facilitate open and cooperative resolutions in compliance-related matters.</p> <p>As discussed in more detail below, we have two primary concerns with the current language in the proposed regulation, in that there is internal ambiguity as to the regulations applicability, as well as an inappropriate standard for determining when an enforcement action is warranted, and the penalties that should apply.</p> <ul style="list-style-type: none"> • <u>Applicability of the Regulation</u> <p>The Preamble of the regulations states that it is being promulgated pursuant to the provisions of Insurance Code section 12921.1 which require the commissioner to establish a program to investigate consumer complaints, and when</p>	<p>The Commissioner has considered the comment and has made a clarifying change, in response to the comment. The comment states that there is an apparent conflict in the proposed regulations. The purported conflict concerns the definition of “enforcement actions” and the applicability of the proposed regulations towards “market conduct examinations or other Department investigations of insurer conduct...” According to the comment, since “enforcement actions” do not include market conduct examinations, the Preamble is in conflict with that definition insofar as it says the proposed regulations will apply to the findings generated in market conduct examinations.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>consumer complaints, and when warranted, initiate enforcement actions based on such investigations. Toward that end, Section 2591.1 provides that:</p> <p style="padding-left: 40px;">“For purposes of this article, enforcement action means any action which is initiated through the issuance of a Notice of Noncompliance, an Order to Show Cause, Accusation, Statement of Issues, or other formal document which alleges a violation to which penalty provisions set forth in any of the statutes listed below apply. For purposes of this article, enforcement actions do not include warning letters, verbal warnings, market conduct exams or market conduct examination reports.” (emphasis added).</p> <p>As such, it would appear that the</p>	<p>The ideas expressed in the comment reflect a misunderstanding regarding how the proposed regulations will operate. The Department, therefore, has revised the language in order clarify the distinction between “market conduct examinations” and “enforcement actions.”</p> <p>An enforcement action is specifically defined in Section 2591.1, subdivision (b). Specifically, these regulations recognize that an “enforcement action” represents only those actions that culminate in the execution of a settlement document and/or an accusatory legal pleading. A market conduct exam is not an “enforcement action”; however, this does not mean that market conduct exams cannot lead to enforcement actions. In other words, the proposed regulations envision that some market conduct examinations may identify conduct that is so egregious that the Department will ultimately apply these regulations and conclude that an enforcement action is appropriate. At this point, these regulations will be reviewed to decide whether or not an enforcement action should take place. In the event that the Department concludes that an enforcement action should take place, a Notice of Noncompliance, Order to Show Cause, Accusation or similar legal pleading shall issue, thereby initiating an “enforcement action.” The proposed regulations recognize that not every market conduct examination will culminate in an “enforcement action” and the regulations distinguish market conduct examinations, warning letters, and verbal warnings for this reason.</p> <p>The Department may often rely upon evidence gleaned from market conduct examinations or other informal investigations in conducting an enforcement action. However, the investigations or examinations</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>provisions of this regulation have no applicability to the settlement negotiations occurring as a result of a market conduct examination.</p> <p>However, the Preamble of the regulations provides that:</p> <p style="padding-left: 40px;">“Pursuant to the commissioner's authority to enforce the Insurance Code, this article shall also apply to the findings generated by other enforcement activities that allege violations of the same statutes and regulations, such as market conduct examinations or other Department investigations of insurer conduct. This article is intended to provide greater uniformity in enforcement and in the general assessment of penalties imposed upon insurers.”</p> <p>Additionally, according to the Statement of Reasons:</p>	<p>are not the enforcement action itself, rather, they are the tools used by the enforcement branch of the Department when conducting enforcement actions. It would be an unnecessary burden for the Department to require the consideration of the guidelines in the proposed regulations when investigating or conducting an exam of an insurance company, issuing a warning letter, or verbal warning. For this reason, the Department has narrowly tailored the scope of the proposed regulations so that they will only apply to those cases that result in a formal enforcement action. The changes to this regulation are intended to clarify this important distinction.</p> <p>The comment suggests that the Department lacks authority to make these regulations applicable to cases other than those that begin through the complaint investigation program described in Insurance Code section 12921.1. The Commissioner has considered the comment and rejects it.</p> <p>Subdivision (b) of proposed regulations section 2591 acknowledges that these regulations are intended to apply to more cases than simply those cases subject to Insurance Code section 12921.1(a)(7). Indeed, the Reference provision and section 2591.1 of the proposed regulations list the penalty provision statutes, which these regulations will implement, interpret and make specific. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department’s authority to promulgate regulations which apply to other investigations of insurer conduct where the Department has inherent authority to implement its regulatory criteria.</p> <p>The penalty statutes listed in the Reference provision and section 2591.1 give the Commissioner authority to impose a penalty from within a range. For example, Insurance Code section 1858.07 authorizes the Commissioner</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>“[The Preamble] is necessary not only because it provides clarity and ease of reference, but also because limiting the regulations to violations discovered in the handling of consumer complaints but not market conduct exams would lead to significant enforcement inconsistencies since market conduct exams identify the same types of violations arising from similar transactions by the same entities. To create such an inconsistency would undermine the value and purpose of the proposed regulations.”</p> <p>As such, the Preamble of the regulation conflicts not only with the specific substantive language of Section 2591.1, but also inappropriately expands the purpose of the regulation, which is limited to the establishment a compliant investigation program pursuant to Section 12921.1 of the California Insurance Code.</p>	<p>For example, Insurance Code section 1858.07 authorizes the Commissioner to impose a penalty “not to exceed” \$5,000 for a non-willful violation and “not to exceed” \$10,000 if the violation is willful. Insurance Code section 12921, subdivision (a) requires the Commissioner to enforce the provisions of the Insurance Code and other laws relating to the business of insurance in this state. The Commissioner has inherent power to implement, interpret and make specific the manner in which these penalty ranges will be applied in practice.</p> <p><i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, “[The Commissioner’s] powers are not limited to those expressly conferred by statute; “rather, ‘[it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.’” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (Italics added.)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>Accordingly, we would respectfully suggest that either the second sentence of Section 2591 – the Preamble – be deleted, or be harmonized with the language in Section 2591.1, to clarify that the regulations applies only to settlement negotiations arising out of compliant investigations.</p>	<p>Here, the proposed regulations will apply to statutes which authorize the Commissioner to seek a penalty “not to exceed” a certain amount. (See, e.g., Ins. Code sections 1858.07 & 10140.5.) It is necessary to promulgate regulations for settlement purposes insofar as the statutes referenced in the proposed regulations authorize the Commissioner to impose penalties within a range, and therefore the Commissioner has inherent authority to create a regulatory scheme to decide appropriate penalties within that range. Furthermore, each agency has inherent (as well as statutory) power to settle cases prior to a hearing, in a manner in which the parties see fit. (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114.)</p> <p>Government Code section 11415.60 recognizes that “[a]n agency may formulate and issue a decision by settlement, pursuant to an agreement of the parties, without conducting an adjudicative proceeding. Subject to subdivision (c), the settlement may be on any terms the parties determine are appropriate.” Subdivision (c) states, in part, “The terms of a settlement may not be contrary to statute or regulation, except that the settlement may include sanctions the agency would otherwise lack power to impose.”</p> <p>Therefore, the Commissioner has broad discretion to adopt rules and regulations as necessary to promote the public welfare. The proposed regulations concern a number of statutes that give the Commissioner the power to impose penalties within a range after a hearing, but the statutes are silent regarding where the appropriate penalty is within the range. We also know that agencies are empowered to settle cases prior to hearing, and that the settlement may include sanctions which do not violate public policy that the agency would otherwise lack the power to impose. It is reasonable for the Commissioner to conclude that, when</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(c)	<p>Standards for Characterizing an Insurer's Conduct as Willful or Knowing</p> <p>More troubling than the internal inconsistency discussed above, is the introduction of a negligence standard when determining whether or not an insurer's actions were a willful or knowing violation of law.</p> <p>Section 2591.3(c)(2) provides that:</p> <p style="padding-left: 40px;">The knowledge or willfulness of the non-compliant act.</p>	<p>settling cases, he will use the statutory penalty ranges as a guideline for deciding what sanctions to impose at settlement. Moreover, the Commissioner's broad discretion to adopt rules and regulations that "may fairly be implied from the statute granting the powers" authorizes him to create guidelines/criteria for enforcement and penalty assessment. (See, generally, <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825.)</p> <p>The authority to adopt these regulations may be fairly implied from those statutes that recognize the agency's inherent power to settle cases "on any terms the parties determine are appropriate." Additionally, the authority to adopt these regulations may be fairly implied from those statutes that designate a penalty range that may be imposed after a hearing.</p> <p>Any inconsistencies existing law are resolved by the following language in Section 2591.1 of the proposed regulations: "To the extent that the provisions of this article conflict with the provisions of any statute or other regulation that more specifically addresses a particular violation, this article shall be inapplicable."</p> <p>It is useful to note that the proposed regulations come into play only when an insurer has violated the law. The regulations do not change existing legal definitions of knowledge or willfulness, or blur the legal definitions of these concepts. The regulations merely indicate that, given there has already been a violation of the law, willfulness as defined in the proposed regulations will be used as a criterion in the Department's deliberations as to whether or not to take an enforcement action and as to the penalty amount. Existing law is utterly silent as to how the Department is to arrive at an exact penalty amount from within the applicable statutory ranges of penalty amounts; there can</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>Violations that may be considered willful or knowingly committed include but are not limited to the following: ***</p> <p>2. When the insurer reasonably should have known of the act's unlawfulness when the non-compliant actions occurred;</p> <p>This language, if retained, would allow the Commissioner to apply a negligence standard when characterizing conduct by an insurer as “willful” or “knowing.” Moreover, it would provide of a definition of “willful” or “knowing” which is in direct conflict with statutory provisions of the Insurance Code defining those terms.</p> <p>At least two sections of the Insurance Code define “willful” as follows:</p>	<p>therefore be no inconsistency in this regard.</p> <p>The regulations reflect a choice by the Department that the exact nature or extent of guilty knowledge on the part of violators will not ordinarily be considered in the Department’s decision making process, once it has been established that a particular statute has been violated. Instead, the criteria listed in Section 2593.1 will form the basis of the Department’s determinations as to which violations will be pursued by enforcement actions. The existing legal distinctions between willful and nonwillful behavior will of course continue to be observed with regard to the determination of whether or not there has in fact been a violation in the first place, both by the Department and by the courts.</p> <p>Contrary to the commenter’s assertions, the broad definition of willfulness in the proposed regulations will not allow for the harshest penalties imposed by the Insurance Code (e.g., those designated for willful violations) to be levied for violations that, according to statute, are not willful. The penalty ranges set forth for willful violations in the statutory penalty provisions being implemented remain higher than those for nonwillful violations. The proposed regulations in this regard only speak to where, within the applicable penalty range prescribed by the legislature, a particular violation is to fall. They do not obliterate existing distinctions in the punishment of willful and nonwillful violations, as the commenter asserts, nor do they make punishment for all violations the same.</p> <p>Given that, in the hypothetical example posed by the commenter, the violation described were indeed nonwillful according to existing law, then even if it were true that the regulations would allow the harshest possible penalty to be imposed for the error, that penalty would still be</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p> “‘Willful’ or ‘willfully’ in relation to an act or omission which constitutes a violation of [the Insurance Code] means with <u>actual knowledge or belief that such act or omission constitutes such violation and with specific intent to commit such violation.</u>” (Ins. S. 12340.9 – Title Insurance, Ins. S. 11750.1 – Workers Compensation Insurance) (emphasis added). </p> <p> In the context of establishing appropriate sanctions for non-compliance with the provisions of the California Insurance Code, the Insurance Code consistently makes distinctions between violations which were willfully or knowingly committed and those that were not. In those instances of willful or knowing violations, harsher sanctions are imposed. To blur the distinctions between “willful” and non-willful violations will undermine the very regulatory </p>	<p> possible penalty to be imposed for the error, that penalty would still be less than if the violation were indeed willful under current law, since the harshest possible penalty would still fall within the lower penalty range specified in statute for a nonwillful violation. If the Department were aware that the violation was not a willful violation under current law, then the penalty range for nonwillful violations would apply, and the regulations would operate to determine the appropriate penalty from within that range. </p> <p> The regulations simply do not, as the commenter asserts, make the punishment for all errors the same. In fact the proposed regulations do distinguish between “simple human error” and knowing violations. Insurers “committed to regulatory compliance” do not generally violate the Insurance Code in circumstances where, according to the language of the proposed Section 2591.3(d)(1)(B) of the amended text, the insurer reasonably should have know of the act’s unlawfulness when the non-compliant act occurred.” </p> <p> Finally, the regulations are in no way “inequitable.” Certainly they do nothing to limit insurers’ due process rights; should an insurer object to the operation of the proposed regulations, it is entitled to proceed to hearing, just as has always been the case. In addition, the definition of willfulness in the proposed regulations is not inequitable in the sense that it is irrational. The Department has chosen in the proposed regulations to make the assumption that a knowing act also involves willfulness for the reason that the Department wished to discourage knowing violations of the Insurance Code. Lastly, there regulations cannot be said to be inequitable because they single out or treat unfairly any one insurer; to the contrary, a central purpose of the regulations is to promote more uniform equitable enforcement of the Insurance Code. </p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>purpose of differentiating willful and non-willful violations, and would allow for the harshest penalties permitted by the Insurance Code to be levied for conduct not contemplated by the Legislature.</p> <p>For example, if a company, when programming its premium notice systems, inadvertently erroneously programs the system such that the premium notices are not issued in exact conformity with regulatory requirements, this regulation would allow the commissioner to find such noncompliance “willful” and impose the harshest penalties possible for the error, since the insurer “reasonably should have known” of the requirements for premium notices. To characterize as “willful” noncompliance something that is nothing more than simple human error, would be unfair and contrary to the purpose of distinguishing between willful and non-willful errors.</p>	<p>uniform, equitable enforcement of the Insurance Code.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>Moreover, when, regardless of a company's true intentions, the punishment for all errors is the same, an environment is created wherein some companies may choose not to dedicate resources to compliance efforts, since such efforts would not provide the value of decreasing a company's exposure to harsh regulatory sanctions.</p> <p>Because it would be inequitable to treat insurers who conduct business in true disregard of their obligations to comply with the provisions of the Insurance Code in the same manner as companies who are committed to regulatory compliance, and because a negligence standard of conduct is inappropriate for determining whether or not a violation was committed "willfully" or "knowingly," we respectfully request that Section 2591.3(c)(2) be deleted from the regulation prior to its promulgation.</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		Once again, we thank you for this opportunity to submit these comments for your consideration and welcome the opportunity to provide any additional information you may find helpful.	
Diane Colborn Vice President of Legislative & Regulatory Affairs Personal Insurance Federation of California 980 Ninth Street, Suite 2030	2591	The Personal Insurance Federation of California submits these comments in response to the notice of proposed adoption of regulations – RH02023676 – regarding enforcement criteria and penalty guidelines. Before addressing the specific sections of the proposed regulations, we have three general comments regarding the authority, consistency, and necessity of the regulations. Authority – Insurance Code Section	The comment suggests that the Department lacks authority to make these

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
<p>Sacramento, CA 95814</p> <p>December 17, 2002</p> <p>Written comments submitted via e-mail and mail.</p>		<p>12921.1(a)(7) gives the Insurance Commissioner specific statutory authority to adopt “a list of criteria to determine which violations should be pursued through enforcement action, and enforcement guidelines that set forth appropriate penalties for violations based on the nature, severity, and frequency of the violations.” The regulatory authority granted to the Department by Section 12921.1(a) is limited to actions arising out of investigations of consumer complaints, and does not extend to other types of investigations, such as market conduct examinations. In contrast, no similar specific legislative mandate exists to adopt regulations governing the criteria for enforcement actions and penalties other than in the consumer complaint context. The department cites to Section 790.10 as an additional source of authority for the broader scope of the proposed regulations beyond the context of consumer complaints. However,</p>	<p>regulations applicable to cases other than those that begin through the complaint investigation program described in Insurance Code section 12921.1. The Commissioner has considered the comment and rejects it.</p> <p>Subdivision (b) of proposed regulations section 2591 acknowledges that these regulations are intended to apply to more cases than simply those cases subject to Insurance Code section 12921.1(a)(7). Indeed, the Reference provision and section 2591.1 of the proposed regulations list the penalty provision statutes, which these regulations will implement, interpret and make specific. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department’s authority to promulgate regulations which apply to other investigations of insurer conduct where the Department has inherent authority to implement its regulatory criteria.</p> <p>The penalty statutes listed in the Reference provision and section 2591.1 give the Commissioner authority to impose a penalty from within a range. For example, Insurance Code section 1858.07 authorizes the Commissioner to impose a penalty “not to exceed” \$5,000 for a non-willful violation and “not to exceed” \$10,000 if the violation is willful. Insurance Code section 12921, subdivision (a) requires the Commissioner to enforce the provisions of the Insurance Code and other laws relating to the business of insurance in this state. The Commissioner has inherent power to implement, interpret and make specific the manner in which these penalty ranges will be applied in practice.</p> <p><i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, “[The Commissioner’s] powers are not limited to those expressly conferred by statute; ‘rather, [it] is well settled in this state that</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>Section 790.10 is only a grant of general authority to adopt regulations that are necessary to administer Article 6.5, the Unfair Practices Act, and does not constitute a specific grant of authority to adopt binding criteria governing future insurance commissioners' determinations regarding enforcement actions and penalties. Moreover, the Insurance Commissioner has not demonstrated that the adoption of these proposed regulations are necessary to administer Article 6.5. For these reasons, we submit that the proposed regulations to the extent they apply to enforcement actions not arising out of consumer complaints exceed the scope of authority granted to the department and are invalid.</p>	<p>[administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ...<i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (Italics added.)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute.</p> <p>Here, the proposed regulations will apply to statutes which authorize the Commissioner to seek a penalty “not to exceed” a certain amount. (See, e.g., Ins. Code sections 1858.07 & 10140.5.) It is necessary to promulgate regulations for settlement purposes insofar as the statutes referenced in the proposed regulations authorize the Commissioner to impose penalties within a range, and therefore the Commissioner has inherent authority to create a regulatory scheme to decide appropriate penalties within that range. Furthermore, each agency has inherent (as well as statutory) power to settle cases prior to a hearing, in a manner in which the parties see fit. (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114.)</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>Government Code section 11415.60 recognizes that “[a]n agency may formulate and issue a decision by settlement, pursuant to an agreement of the parties, without conducting an adjudicative proceeding. Subject to subdivision (c), the settlement may be on any terms the parties determine are appropriate.” Subdivision (c) states, in part, “The terms of a settlement may not be contrary to statute or regulation, except that the settlement may include sanctions the agency would otherwise lack power to impose.”</p> <p>Therefore, the Commissioner has broad discretion to adopt rules and regulations as necessary to promote the public welfare. The proposed regulations concern a number of statutes that give the Commissioner the power to impose penalties within a range after a hearing, but the statutes are silent regarding where the appropriate penalty is within the range. We also know that agencies are empowered to settle cases prior to hearing, and that the settlement may include sanctions which do not violate public policy that the agency would otherwise lack the power to impose. It is reasonable for the Commissioner to conclude that, when settling cases, he will use the statutory penalty ranges as a guideline for deciding what sanctions to impose at settlement. Moreover, the Commissioner’s broad discretion to adopt rules and regulations that “may fairly be implied from the statute granting the powers” authorizes him to create guidelines/criteria for enforcement and penalty assessment. (See, generally, <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825.)</p> <p>The authority to adopt these regulations may be fairly implied from those statutes that recognize the agency’s inherent power to settle cases “on any terms the parties determine are appropriate.” Additionally, the authority to adopt these regulations may be fairly implied from those statutes that designate a penalty range that may be imposed after a hearing.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>designate a penalty range that may be imposed after a hearing.</p> <p>To the extent that this comment suggests the proposed regulations duplicate, or are inconsistent with the Fair Claims settlement practices regulations, the Commissioner has considered and rejects the comment. The comment does not cite any specific examples where there is an inconsistency between the proposed regulations and the Fair Claims settlement practices regulations.</p> <p>At least one commenter has argued that the proposed regulations do not meet the necessity standard, in light of the fair claims settlement practices regulations. This comment has been considered and is rejected. First, in the context of consumer complaints, the proposed regulations are necessary because Insurance Code section 12921.1(a)(7) expressly requires that we promulgate them.</p> <p>As the commenter notes, however, the Department has decided to promulgate these regulations for use in conducting enforcement actions that are initiated for reasons other than consumer complaints. Examples of the kinds of situations where the proposed regulations would also apply include enforcement actions, which are based upon the findings of a market conduct examination or other Department investigation. Regardless of whether the Department conducts an enforcement action based upon the findings of a market conduct examination, a Department investigation, or in response to a consumer complaint, the decision regarding the appropriate penalty and whether to bring an enforcement action is the same. Therefore, the proposed regulations must cover more contexts than merely those cases where a consumer complaint has led to an enforcement action. If the proposed regulations did not apply to the</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>Consistency – Application of these proposed regulations to claims practices violates the consistency standard to the extent they are inconsistent with existing provisions of the fair claims practices regulations governing enforcement actions and penalties. Title 10, Section 2695.12, sets forth criteria and guidelines for determining acts of noncompliance and appropriate penalties. These existing regulations differ from the proposed regulations in several substantive ways. To the</p>	<p>findings from market conduct examinations or investigations, this would raise a potential consistency problem. The regulations would be inconsistent because, by all accounts, enforcement actions and penalties are imposed in exactly the same way, regardless of whether they are initiated by a consumer complaint, the findings of a market conduct exam, or a Department investigation. Yet, by making the proposed regulations apply solely to consumer complaints, they could lead to inconsistent enforcement of actions, which arise under other circumstances. For the reasons mentioned above, the proposed regulations must necessarily apply to other situations where the Department discovers – through a market conduct exam, investigation, or other non-consumer-complaint context – that an enforcement action is needed.</p> <p>Any inconsistencies with the Fair Claims Settlement Practices regulations are resolved by the following language in Section 2591.1 of the proposed regulations: “To the extent that the provisions of this article conflict with the provisions of any statute or other regulation that more specifically addresses a particular violation, this article shall be inapplicable.”</p> <p>Nonetheless, there are no significant inconsistencies with the Fair Claims Settlement Practices regulations. The commenter’s assertion that “the existing regulations differ from the proposed regulations in several substantive ways” is without basis in fact, which is why the commenter cannot identify even one such inconsistency. The only possible area of overlap involves Cal. Code Regs, tit. 10, §2695.12,</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>extent the proposed regulations are intended to apply to claims practices and are inconsistent with Section 2695.12, they fail to meet the consistency standard. Government Code Section 11342.2 provides that regulations to be valid must be consistent and not in conflict with statute, and reasonably necessary to effectuate the purpose. Government Code Section 11349 similarly requires that regulations be consistent and not in conflict with existing statutes, court decisions, and other provisions of law. To the extent that the regulations overlap or duplicate provisions of the fair claims practices regulations, they also fail to meet the nonduplication standard as specified in Government Code Section 11349.</p>	<p>subds. (b) and (c). In subdivision (b), a list of the types of admissible evidence is provided which the Commissioner will consider in determining appropriate penalties. However, the list is not an exclusive list, and the kinds of evidence that according to the existing regulation are to be considered are indeed entirely consistent with the criteria set forth in the proposed regulations. Subdivision (c) indicates, in pertinent part, that in determining penalties to be assessed under the Unfair Claims Settlement Practices regulations, that the Commissioner “shall not consider reasonable mistakes or opinions as to valuation of property, losses or damages.” Cal. Code Regs, tit. 10, §2695.11, subd. (c). It is conceivable that, in the claims valuation context only, this language could be at odds with Section 2591.3(d)(a)(B) of the revised text of regulations. If there were indeed an inconsistency, then Section 2591.1 of the proposed regulations makes it clear that the proposed regulations would be inapplicable, to the extent of the inconsistency, as noted above. However, it is unclear how “reasonable mistake[s]” such as those excepted from consideration under the existing regulations could ever be considered knowledgeable or willful under the proposed regulations for the reason that “the insurer reasonably should have known of the act’s unlawfulness when the non-compliant act occurred.” It seems logical that if the insurer reasonably should have known of an act’s unlawfulness, then such an act could not fairly be considered a reasonable mistake. The proposed regulations therefore do not run afoul of the Administrative Procedure Act's consistency standard.</p> <p>As for the nonduplication standard, the proposed regulations simply do not duplicate either the language or the substance of the Unfair Claims Settlement Practices regulations, which is why the commenter again can provide no basis for the assertion that they do. Cal. Code Regs, tit. 10</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>Necessity – While we agree with the laudable goal cited by the department of providing for greater uniformity in enforcement and assessment of penalties, we are concerned that the regulations appear to replace the discretion and flexibility currently vested in the commissioner with mandatory standards that could be interpreted to require the department to assess certain penalties and take enforcement actions. The Insurance Commissioner should be allowed to exercise discretion and flexibility in determining which enforcement actions to pursue and the level of penalties to assess, based on a case by case evaluation, and the commissioner’s determination of whether an enforcement action, or per-act penalties, are warranted and in</p>	<p>provide no basis for the assertion that they do. Cal. Code Regs, tit. 10, §2695.11, subd. (b) lists kind of admissible evidence that are to be considered; Section 2591.3 of the proposed regulations list criteria that are to be considered. Since the commenter provides no specific examples of either inconsistencies or duplications, it is difficult to understand how the proposed regulation can at once duplicate and be inconsistent with the existing one.</p> <p>The Commissioner has considered the comment and rejects it. The Department conducts a wide range of activities designed to bring insurers into compliance with the many requirements of the Insurance Code. Aside from those instances where a penalty is mandated by statute for a given offense, it is neither feasible nor prudent to impose penalties upon every observed violation, no matter what the underlying circumstances reveal. The Legislature expresses a penalty provision in mandatory terms, when it intends for a state agency to impose a penalty without discretion. The logical corollary to this rule is that those penalties, which are not mandatory may be imposed at the discretion of the Department.</p> <p>The Department routinely takes steps to force insurers into compliance with the Insurance Code using methods that do not necessarily result in a formal enforcement action. For example, when the circumstances surrounding a market conduct examination suggest that a company is prepared to make amends for potentially inappropriate or illegal rating and underwriting, the Department has the discretion to expedite the return of premium for consumers, rather than engage in a costly and time-consuming enforcement action.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>the best interests of consumers and the competitive market. However, the regulations would appear to mandate such actions by providing that the commissioner “shall” take enforcement actions and “shall” assess penalties for <u>each act</u>.</p> <p>These concerns have been ameliorated to some extent with the addition of language in Section 2591.4 which gives the commissioner the flexibility and discretion in determining whether to pursue an enforcement action and to consider other factors in addition to those listed, and to determine which of those factors listed are relevant under the circumstances. This language is helpful but appears inconsistent with language in Section 2591.2 which states that the commissioner <u>shall</u> consider the criteria listed in Section 2591.3, and if he or she determines a penalty is warranted <u>shall</u> impose a penalty for each act.</p> <p>The language in Section 2591.1 clarifies that these regulations do not</p>	<p>For that matter, in those cases that do require enforcement proceedings, one critical component of any enforcement action is the option of settlement. Settlements, by their very nature, represent a compromise between the parties. Settlement may be the most prudent option when, for example, a statute that is the basis for a violation is reasonably susceptible to more than one meaning. Similarly, the circumstances of a particular insurer or its policyholders may require that the insurer pay penalties of a lesser or greater amount than typically imposed.</p> <p>It is the position of the Department that judgment and equity must enter into any decision to conduct an enforcement action or assign an appropriate penalty. The proposed regulations provide instructions to the Department and the public, which will promote the equitable and consistent enforcement of the Insurance Code. The proposed regulations are very flexible and are designed to preserve the Commissioner’s flexibility in deciding which enforcement actions should be taken and how much penalty should be imposed. This is why proposed regulations Section 2591.4 allows the Commissioner to decide the relevance of each criterion and to apply unstated criteria, when circumstances warrant.</p> <p>With regard to the commenter’s concerns with regard to the “shall” and for “each act” language in section 2591.2, the Commissioner has considered the comment and the regulation has been modified to read as follows: “[i]f after a review of those criteria the Department determines that an enforcement action is warranted, the Department shall take into consideration the criteria listed in Section 2591.3 and any other relevant considerations to determine an appropriate penalty for each act in violation of the law from within the applicable statutory penalty range or</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>apply to settlement conferences ordered pursuant to the APA. In addition, Section 2591.4 does appear to allow the commissioner to take other considerations into account in reaching a settlement agreement, as long as the basis for such considerations are stated to the insurer during the settlement negotiations. These are good clarifications. Nevertheless, we are concerned that the mandatory language of Section 2591.2 and 2591.3 could be interpreted to preclude settlement agreements between the department and an insurer that would allow for alternative remediation and compliance in lieu of the potentially severe penalties mandated in the Regulations for “each act,” when it is determined by the commissioner that such an alternative remedy is more appropriate under the circumstances. To the extent the commissioner is forced to initiate enforcement actions and to assess large penalties instead of negotiating a settlement agreement, this in turn will lead to</p>	<p>violation of the law from within the applicable statutory penalty range or ranges.” If it is then determined that a penalty is warranted then the Commissioner shall impose one. The language of section 2591.4 is not inconsistent with language in section 2591.2 as the commenter suggests. Regarding a mandate that enforcement actions and penalties shall be taken for “each act”, it is the position of the Department that judgment and equity must enter into any decision to conduct an enforcement action or assign an appropriate penalty. The proposed regulations provide instructions to the Department and the public, which will promote the equitable and consistent enforcement of the Insurance Code.</p> <p>The proposed regulations do not force the commissioner to “assess large penalties,” rather, the regulations expressly recognize that they are for use in negotiating a settlement. In fact, it is the position of the Department that judgment and equity must enter into any decision to conduct an enforcement action or assign an appropriate penalty. The proposed regulations provide instructions to the Department and the public, which will promote the equitable and consistent enforcement of the Insurance Code. The proposed regulations are very flexible and are designed to preserve the Commissioner’s flexibility in deciding which enforcement actions should be taken and how much penalty should be imposed. This is why proposed regulations Section 2591.4 allows the Commissioner to decide the relevance of each criterion and to apply unstated criteria, when circumstances warrant. The proposed regulations are not intended to increase or decrease the number of enforcement actions that are initiated. Nor are the proposed regulations designed to impose “large penalties.” These regulations, are merely designed to provide the public and the Department with guidelines to consider when conducting enforcement actions and imposing penalties.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.2	<p>more appeals by insurers, and more administrative hearings and court actions. Increased litigation of alleged violations is not necessarily the best use of regulatory resources, and such rigid application of enforcement criteria is not necessary to implement the law.</p> <p>Specific Section by Section Comments</p> <p>Section 2591.2 – The unnecessary restriction on commissioner discretion and flexibility cited above could be partially remedied by amending the third sentence of this paragraph by changing the word “shall” to “may” so that the sentence would read as follows: “If, after a review of those criteria the commissioner determines that a penalty is warranted, the commissioner <u>may</u> shall impose a penalty for each act against a consumer or other licensee in violation of the law from within the applicable penalty range.”</p>	<p>The Commissioner has considered the comment and the regulation has been modified to read as follows: “[i]f after a review of those criteria the Department determines that an enforcement action is warranted, the Department shall take into consideration the criteria listed in Section 2591.3 and any other relevant considerations to determine an appropriate penalty for each act in violation of the law from within the applicable statutory penalty range or ranges.” If it is then determined that a penalty is warranted then the Commissioner shall impose one. The commenter suggests there is an unnecessary restriction on commissioner discretion and flexibility that could be partially remedied by amending the proposed regulation. The language of the proposed regulations is not restrictive and inflexible: the intended purpose of the regulations is to create greater consistency in the enforcement process but allowing the necessary flexibility to determine the appropriate penalty.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>The last sentence of that paragraph states that in addition to the penalty amount, the Department may also recover its costs associated with the enforcement action. It is unclear what the authority is for this provision. The regulations do not cite the authority for this provision, and it does not appear to be authorized by Section 12921.1.</p>	<p>The Commissioner has considered the comment and respectfully rejects it. There is statutory authority for the Department to recover enforcement costs or attorney’s fees from an insurer against whom an enforcement action has been taken. The reference note to section 2591.2 includes both CIC 12921, as well as the Department’s rulemaking authority, CIC section 12921.1. Section 12921.1 expressly grants the Department authority to write regulations concerning consumer complaints. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department’s authority to promulgate regulations which apply to other investigations of insurer conduct where the Department has inherent authority to implement its regulatory criteria. <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, “[The Commissioner’s] powers are not limited to those expressly conferred by statute; “rather, “[it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.’” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (Italics added.)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court in those cases was describing the inherent</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(a)(2)	<p>Section 2591.3(a)(2) – Although in other places consideration of criteria is mandated by these contemplated regulations, in this case the regulations would make consideration of the complexity of the transaction optional by use of the term “may.” This is inconsistent with the</p>	<p>California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute. Section 2591 expressly recognizes that the regulations are to be used for settlement purposes. The reference note to section 2591.2 includes CIC 12921. Section 12921(b)(4) specifically states that “[I]n an administrative action to enforce the provisions of this code and other laws regulating the business of insurance in this state, any settlement is subject to...: a settlement may include the sanctions provided by this code or other laws regulating the business of insurance in this state, except that the settlement may include <i>attorney’s fees, costs of the department in bringing the enforcement action, and future costs of the department to ensure compliance with the settlement agreement</i>” (emphasis added). Since it is intended that the provisions of section 2591 are appropriate for determining the penalty imposed in those cases that are resolved through <i>settlement</i> authority exists to recover enforcement costs or attorney’s fees from an insurer against whom an enforcement action has been taken. Therefore, no change will be made.</p> <p>The Commissioner has considered the comment and respectfully rejects it. The Fair Claims Settlement Practices regulations state that the commissioner “can” consider certain factors. The proposed regulations state that the Commissioner “shall” consider certain enumerated factors. It is useful to note that the proposed regulations come into play only when an insurer has violated the law. The regulations presuppose that there has been a violation: “The Department shall examine the violations committed by the insurer”</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(b)	<p>fair claims settlement regulations which require the commissioner to consider the complexity of the claim in determining noncompliance and appropriate penalties.</p> <p>Section 2591.3(b) – In this subsection it is unclear how the department will reasonably determine how many persons have been impacted by a violation. This provision may make sense in the context of a market conduct examination where sampling of claims may be involved, but does not appear to be applicable in the context of an individual consumer complaint or complaints. Since the department’s authority for the regulations is limited to investigations arising out of consumer complaints, as stated above, it is recommended that this section be stricken. If this section is</p>	<p>(Section 2591.2 of the amended text of the proposed regulations). The regulations merely indicate that, given there has already been a violation of the law, no such distinction will be made in the Department’s deliberations as to whether or not to take an enforcement action and as to the penalty amount. There may be a conflict at the penalty phase since there is a very minor difference between “shall” and “may”. However, if it is determined that there is indeed a conflict then section 2591.1 would come into play expressly providing that the regulations are inapplicable when they conflict with the provisions of any statute or other regulation that more specifically addresses a particular violation. Therefore, no change will be made.</p> <p>The commenter states it is unclear how the Department will reasonably determine how many persons have been impacted by a violation. The language of the proposed regulation is such that even in a case with no widespread impact, the proposed regulation is still applicable. As is explained above, the Department’s authority for the proposed regulations is not limited to investigations arising out of consumer complaints. The commenter suggests inserting the word “detrimentally” before the word “impacted”. Such a change will not be made because impact to the individual does not have to be detrimental.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(c)	<p>retained, we recommend that the word “detrimentally” be inserted before the word “impacted” on line three.</p> <p>Section 2591.3(c) – This section fails to meet the clarity standard and confuses the term “willful” with “knowing”, and the terms “willful and knowing” with negligence. For instance, the regulation provides that willful or knowing violations include violations where the insurer reasonably “should have known.” “Willful” and “should have known” are not the same standard but are treated the same under the regulations. The phrase “should have known” implies negligence, not willfulness. The regulations in effect make all violations “willful” by definition. Such a standard is entirely inappropriate. Moreover, attributing the actions of an employee to an insurer as “willful” violations unless</p>	<p>Contrary to the commenter’s assertion, this subdivision does not violate the clarity standard of the Administrative Procedure Act. The language is precise, and no unclear language has been identified. In fact, the regulations provide detailed descriptions of the kinds of behavior that will be considered willful or knowing.</p> <p>It is useful to note that the proposed regulations come into play only after an insurer has violated the law. The regulations do not change existing legal definitions of knowledge or willfulness, or blur the legal definitions of these concepts. The regulations merely indicate that, given there has already been a violation of the law, knowledge/willfulness as defined in the proposed regulations will be used as a criterion in the Department’s deliberations as to whether or not to take an enforcement action and as to the penalty amount. Existing law is utterly silent as to how the Department is to arrive at an exact penalty amount from within the applicable statutory range of penalty amounts; there can therefore be no inconsistency in this regard.</p> <p>The regulations reflect a choice by the Department that the exact nature or extent of guilty knowledge on the part of violators will not ordinarily be considered in the Department’s decision making process, once it has been established that a particular statute has been violated. Instead, the</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		the employee acted outside the scope of employment or “otherwise not in the interest of the insurer” is an ambiguous standard and effectively means that actions of employees will almost always be attributed to the insurer as “willful” violations, even where such actions were not authorized or condoned by the insurer.	<p>criteria listed in Section 2591.3 will form the basis of the Department’s determinations as to which violations will be pursued by enforcement actions. To the extent they are relevant, the existing legal distinctions among negligent, knowing, willful and nonwillful behavior will of course continue to be observed with regard to the determination of whether or not there has in fact been a violation in the first place, both by the Department and by the courts.</p> <p>Any potential ambiguity arising from the phrase, “otherwise not in the interest of the insurer,” has been eliminated in the Amended Text of Regulation, since this language has been deleted.</p> <p>The proposed regulations do not come into play until there has been a violation of California law, namely the Insurance Code, by an insurer.</p> <p>Contrary to the commenter’s assertions, the proposed regulations’ definition of willfulness does not mean “that actions of employees will almost always be attributed to the insurer as ‘willful’ violations.” Insurers that according to existing law have not committed a willful violation are not currently, and under the proposed regulations will not be, penalized on account of the willful acts of their agents for violating a statutory provision requiring willfulness. Again, the proposed regulations only come into play once there has been a violation of the Insurance Code. Once there has been such a violation, however, the proposed regulations indicate only that willfulness on the part of an insurer’s agents will be ascribed to the insurer for the purposes of determining whether or not to pursue through enforcement action that violation and determining the exact penalty amount to be sought from within the applicable range.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(e)	<p>Section 2591.3(e) – This subsection provides that the compliance record of the insurer shall be considered and that the compliance record includes the number and types of violations identified in the investigation of consumer complaints generated by the insurer in the previous time period, as specified. However, the regulations do not specify whether this is to be based on raw numbers alone, regardless of the size of the company or the number of claims handled. The size of the company and the total volume of claims handled is</p>	<p>It is true that this criterion does tend to hold insurers accountable for violations committed willfully by their agents. And, all other things being equal, it is reasonable to do so; as between two insurers whose violations make them subject to the same penalty provision and which are in all other respects similar, it is a reasonable exercise of discretion to initiate an enforcement action against, or impose a higher penalty from within the applicable range on, the insurer whose agents acted willfully as opposed to the insurer whose agents did not. However, the proposed language simply does not cause a violation that does not meet existing legal requirements for willfulness to become a willful violation.</p> <p>The commissioner has considered this comment and rejects it. One of the purposes of this criterion is to provide the commissioner with the necessary flexibility to put the violation into context with the overall compliance behavior of the insurer. Company size will not always be a consideration because the regulations are not intended to operate to give larger companies the opportunity to escape liability based upon their size. That is, the regulations are not intended to provide insurers with a means of determining when it will be to their benefit to violate the law. Insurers are to avoid all violations of the Insurance Code.</p> <p>Additionally, although the regulation does not specify how a compliance record will be determined, the regulation does not preclude the Department from considering size of the company or the number of claims handled. To place specific, objective parameters in this criterion would necessarily take away the commissioner’s discretion and</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(f)	<p>obviously important in determining the relevance of the number of complaints and violations.</p> <p>Section 2591.3 (f) -- This provision does not specify over what period of time the measurement of “duration” will be made. In addition, in determining whether a violation is a single or repeated event, unintentional, systems-generated errors should not be considered a repeat violation but a single event. The regulations do not seem to address this likelihood, other than in considering the willfulness of the violation. However, since the penalty per act is established first, the overall penalty may be unreasonable given the nature of the violation. The regulations should provide for tempering or reduction of penalty assessments in the case of violations which result from mechanical processes or other systems-generated errors.</p>	<p>negate part of the purpose of this criterion. Lastly, company size may also be addressed under the frequency criterion.</p> <p>The commissioner has considered this comment and rejects it. The regulations provide the commissioner with necessary flexibility to put the violation at hand in context with the overall behavior of the insurer. The language of the regulation does specify the time period over which duration will be made as the duration of the noncompliant activity. Computer or mechanical generated errors should not always be treated as one error they may be reflective of the insurer’s lack of quality control or attention to compliance. Lastly, there is nothing in the text of the regulation precluding the Department from treating a computer error as a single error when appropriate. The current language allows the commissioner to dismiss or lessen penalties for short-lived transgressions resulting from a minor oversight or a quickly corrected behavior. This current language of this criterion also provides the commissioner with the flexibility needed to review the context of the violation and in determining whether an enforcement action is necessary in order to achieve future compliance by the insurer or whether the noncompliance was an aberration that, once corrected, is not likely to be repeated.</p>
	2591.3(g)	<p>Section 2591.3 (g) – This provision addresses “extraordinary</p>	<p>The commissioner has considered this comment and rejects it. To the degree the violation is beyond the insurer’s control, it is reasonable to</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(h)	<p>circumstances” outside the control of the insurer. We recommend that this subsection be amended to provide that extraordinary circumstances shall include but not be limited to a disaster or emergency declared by the governor or president.</p> <p>Section 2591.3 (h) – This subsection requires the commissioner to consider previous actions taken by the commissioner against other insurers. Without knowing whether previous enforcement actions against other insurers were fair or not, this subsection raises significant due process concerns.</p>	<p>provide the commissioner with the flexibility to recognize that an enforcement action may be an unwarranted punishment and meaningless as a deterrent against future noncompliance. However, not all disasters or emergencies declared by the governor or president should be considered extraordinary circumstances. Disasters or emergencies can include those for which an insurer specifically provides coverage such as earthquakes. An earthquake may be declared an emergency however, if the insurer provides earthquake insurance, the insurer will not be excused from its legal obligations simply because an earthquake actually occurs. The inclusion of extraordinary circumstances as a consideration allows the commissioner to choose to refrain from an enforcement action or to lessen the amount of the penalty imposed irrespective of other criteria when the violation results in whole or in part from circumstances beyond the insurer’s control.</p> <p>The Commissioner has considered this comment and rejects it. This criterion is consistent with the intended purpose of the regulations of creating greater consistency in the enforcement process but allows the necessary flexibility to escalate the penalty if previous penalties assessed for similar non-compliance are not producing the desired deterrent effect.</p> <p>The purpose of the proposed regulation is to implement enforcement actions and penalties consistently, fairly and equitably. To that end, the proposed regulation provides that the commissioner may take into account previous actions against insurers of similar size and circumstance. This criterion also allows the commissioner to reevaluate the noncompliance and determine a penalty irrespective of previous penalty amounts if needed. The language is not contradictory but rather provides the Commissioner with flexibility as well as meeting the goal of</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.4	<p>Section 2591.4 – This paragraph includes helpful language which acknowledges the need for flexibility for the Insurance Commissioner to exercise discretion in determining which criteria are relevant under the circumstances. The requirement that the basis for other considerations be stated during the settlement negotiations is also appropriate. However, this requirement should be broadened to require the Insurance Commissioner to state</p>	<p>consistency.</p> <p>For the purposes of these regulations, it is not necessary for an insurer to judge the “fairness” of prior enforcement and penalty actions. There is no due process issue as the regulations do nothing to limit insurers’ due process rights; should an insurer object to the operation of the proposed regulations, it is entitled to proceed to hearing, just as has always been the case. It is not the intent of the proposed regulations, or the statutes they implement, to give would-be violators advice in advance as to which of their violations will or will not be pursued through enforcement actions or receive stiff penalties. That is, the regulations are not intended to provide insurers with a means of determining when its will be to their benefit to violate the law. Insurers are to avoid all violations of the Insurance Code.</p> <p>We agree: The paragraph is indeed helpful. However, there is simply no legal requirement that the Commissioner state which considerations were taken into account in arriving at a penalty amount. Such a requirement would be unduly burdensome. Further, the commenter provides no reasoning to support the assertion that such a statement should be required.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>which of all the considerations were taken into account in arriving at a penalty, not just those considerations not listed in the guidelines.</p> <p>Thank you for the opportunity to comment on the proposed regulations. If you have any questions regarding these comments, please let me know.</p>	
<p>Robert W. Hogeboom and Robert J. Cerny on behalf of Barger and Wolen, L.L.P.</p> <p>515 S. Flower Street 34th Floor Los Angeles, CA 90071</p>		<p>On August 22, 2003, the California Department of Insurance (“Department”) issued a Notice of Availability of Revised Text, inviting public comment on revisions to contemplated Regulations for Enforcement Action and Penalties (the “Regulations”). The Regulations set forth guidelines and factors for the Department to consider in bringing enforcement actions and assessing penalties in settlement negotiations. On December 17, 2002, we presented comments and objections to the previous version of the Regulations, a copy of which is attached as</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
Written comments submitted via e-mail September 8, 2003		<p>Exhibit A, arguing that the Regulations lack authority, are unnecessary and unclear in various respects. We incorporate those comments herein, as the revised text has not remedied many of the flaws that we pointed out previously, and we have limited these comments to the revisions presented on August 22, 2003.</p> <p>With respect to the revisions, we respectfully request that the Commissioner reconsider the text for the following reasons:</p> <p>(1) Revisions to Section 2591 do not remedy the Commissioner’s lack of authority to promulgate enforcement and penalty regulations that extend to actions other than consumer complaints.</p> <p>(2) Language added to Section 2591.4 regarding mitigation is inconsistent with other language in the Regulations and would</p>	

¹⁰ “Necessity” means that record of the rulemaking proceeding demonstrates by substantial evidence the need for the regulation to effectuate the purpose of the statute that the regulation implements, interprets or makes specific. Cal. Gov’t Code § 11349(a).

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591(b)	<p>render the Regulations inflexible and unworkable. (3) Revisions to the Regulations have not added clarity and will not promote uniformity in enforcement actions and penalties. (4) The revised Regulations still improperly attribute knowledge and willfulness to the insurer without evidence of actual knowledge or willfulness.</p> <p><u>1. LEGAL AUTHORITY</u></p> <p><i>Revisions to the Regulations’ preamble have not remedied the Regulations’ lack of authority, as they still purport to apply to enforcement actions not arising out of consumer complaints.</i></p> <p>As explained in our previous comments, the scope of the Regulations should be limited to</p>	<p>This comment is simply a reiteration of the comment provided by the same commenter during the 45-day comment period. However, the commenter now states that the revisions to the proposed regulations, which purportedly broaden their application, do not remedy the commenter’s belief that the Department lacks authority to promulgate these regulations. Specifically, the comment suggests that the Department lacks authority to make these regulations applicable to cases other than those that begin through the complaint investigation program described in Insurance Code section 12921.1. The Commissioner has considered the comment and rejects it.</p> <p>The comment suggests that the Department lacks authority to make these regulations applicable to cases other than those that begin through the complaint investigation program described in Insurance Code section 12921.1.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>consumer complaints under the authority of Insurance Code section 12921.1, which requires the Commissioner to establish a program to investigate and respond to consumer complaints and to bring enforcement actions against insurers when warranted. While the Commissioner has made several adjustments to Section 2591(b), which expands the scope of the Regulations to actions not arising from complaints, the revisions have not fixed that basic flaw. Therefore, the Regulations exceed the scope of the Commissioner's authority.</p>	<p>Subdivision (b) of proposed regulations section 2591 acknowledges that these regulations are intended to apply to more cases than simply those cases subject to Insurance Code section 12921.1(a)(7). Indeed, the Reference provision and section 2591.1 of the proposed regulations list the penalty provision statutes, which these regulations will implement, interpret and make specific. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department's authority to promulgate regulations which apply to other investigations of insurer conduct where the Department has inherent authority to implement its regulatory criteria.</p> <p>The penalty statutes listed in the Reference provision and section 2591.1 give the Commissioner authority to impose a penalty from within a range. For example, Insurance Code section 1858.07 authorizes the Commissioner to impose a penalty "not to exceed" \$5,000 for a non-willful violation and "not to exceed" \$10,000 if the violation is willful. Insurance Code section 12921, subdivision (a) requires the Commissioner to enforce the provisions of the Insurance Code and other laws relating to the business of insurance in this state. The Commissioner has inherent power to implement, interpret and make specific the manner in which these penalty ranges will be applied in practice.</p> <p><i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, "[The Commissioner's] powers are not limited to those expressly conferred by statute; 'rather, '[it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>powers.’” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (Italics added.)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute.</p> <p>Here, the proposed regulations will apply to statutes which authorize the Commissioner to seek a penalty “not to exceed” a certain amount. (See, e.g., Ins. Code sections 1858.07 & 10140.5.) It is necessary to promulgate regulations for settlement purposes insofar as the statutes referenced in the proposed regulations authorize the Commissioner to impose penalties within a range, and therefore the Commissioner has inherent authority to create a regulatory scheme to decide appropriate penalties within that range. Furthermore, each agency has inherent (as well as statutory) power to settle cases prior to a hearing, in a manner in which the parties see fit. (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114.)</p> <p>Government Code section 11415.60 recognizes that “[a]n agency may formulate and issue a decision by settlement, pursuant to an agreement of the parties, without conducting an adjudicative proceeding. Subject to</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.4(a)	<u>2. THE REGULATIONS ARE INCONSISTENT</u>	<p>subdivision (c), the settlement may be on any terms the parties determine are appropriate.” Subdivision (c) states, in part, “The terms of a settlement may not be contrary to statute or regulation, except that the settlement may include sanctions the agency would otherwise lack power to impose.”</p> <p>Therefore, the Commissioner has broad discretion to adopt rules and regulations as necessary to promote the public welfare. The proposed regulations concern a number of statutes that give the Commissioner the power to impose penalties within a range after a hearing, but the statutes are silent regarding where the appropriate penalty is within the range. We also know that agencies are empowered to settle cases prior to hearing, and that the settlement may include sanctions which do not violate public policy that the agency would otherwise lack the power to impose. It is reasonable for the Commissioner to conclude that, when settling cases, he will use the statutory penalty ranges as a guideline for deciding what sanctions to impose at settlement. Moreover, the Commissioner’s broad discretion to adopt rules and regulations that “may fairly be implied from the statute granting the powers” authorizes him to create guidelines/criteria for enforcement and penalty assessment. (See, generally, <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825.)</p> <p>The authority to adopt these regulations may be fairly implied from those statutes that recognize the agency’s inherent power to settle cases “on any terms the parties determine are appropriate.” Additionally, the authority to adopt these regulations may be fairly implied from those statutes that designate a penalty range that may be imposed after a hearing.</p> <p>There is no inconsistency. Nothing in Section 2591.3 indicates that lack of harm is to mitigate the effect of any relevant criterion, nor is there a</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p><i>New language in Section 25914(a) would prevent the Department from considering mitigation for lack of harm or the inapplicability of one or more criteria. This is inconsistent with Section 2591.3, which clearly provides for mitigation for lack of harm and requires the Department to consider lack of applicability of other criteria.</i></p> <p>Section 2591.4 has been revised to provide:</p> <p>“(a) Equal consideration need not be given to each criterion described in these guidelines <u>Section 2591.3</u>. The commissioner <u>Department</u> shall determine which criteria are relevant under the circumstances and shall determine the appropriate consideration to be given to those criteria. <u>Neither</u></p>	<p>of harm is to mitigate the effect of any relevant criterion, nor is there a requirement that the Department consider lack of applicability of other criteria, which is why the commenter can point to no specific language to this effect in Section 2591.3. Nonetheless, the new (Section 2591.4(a)) language complained of here is necessary, as demonstrated by the submission of this comment, in order to preempt the very sort of creative argument the commenter makes here, when the proposed regulations are put into effect. The Department, as the new language makes unmistakably clear, will not consider criteria that are not applicable, and absence of harm will not mitigate the effect of any relevant criteria.</p> <p>Extent of harm is an indicator of the severity of the violation criterion; however, in order for this indicator to be operative, there must be facts indicating harm. Absence of such facts, on the other hand, simply means that this indicator is not triggered; it does not mean that an insurer committing a violation that is otherwise severe is essentially to be rewarded just because there has been no showing of harm. If the regulations indicated otherwise, insurers could be incentivized to commit violations in instances where there could be no such showing, if they thought they could predict that such violations would not be subject to enforcement actions or stiff penalties.</p> <p>There are mitigating factors in the proposed regulations, but they in each case are applicable only when affirmative facts trigger those criteria. Contrary to the commenter’s assertion, the new language makes the regulations more, not less, “workable.” If one were to accept the commenter’s logic, the regulations, without the new language, would require the Department to consider all the facts <i>not</i> present in connection with each violation. This would indeed be an unworkable situation.</p> <p>The commenter quotes accurately from the language of Section 2591.3,</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p><u>inapplicability of one or more criteria nor the absence of harm shall mitigate the effect of any relevant criterion.”</u></p> <p>The addition of the last sentence in the above paragraph renders the regulation inconsistent and unworkable. Section 2591.3 lists the criteria that the Department must consider in determining that an enforcement action is warranted and in selecting a penalty. Section 2591.3 requires the Department to consider the severity of the violation, which essentially measures the amount of harm caused by the alleged violation. For example, subsection (b)(1)(A) lists the following as an element of severity: “the extent of harm revealed through a consumer complaint ...” In addition, subsection (c) regarding frequency requires the identification of the persons “reasonably determined to have been <i>impacted</i>” by the alleged violation. (Emphasis added). Accordingly, presence or absence of harm is an important consideration contained in many of</p>	<p>but then draws a conclusion not based on the quoted language. It simply does not follow from the cited material that absence of harm “should” or “must” mitigate the effect of any relevant criterion.</p> <p>The assertion that the new language renders the proposed regulations “incomprehensible” is false. There is simply nothing in the regulations to support the claim that “Where an important criterion does not apply, the Department may decide to reduce the penalty.” Only applicable criteria will be considered. And, because it is not beyond the realm of possibility that the regulations in their originally noticed form would leave open the possibility of another interpretation, the new language is necessary to foreclose any such other interpretation: The new language makes it clear that inapplicable criteria will not be considered.</p> <p>Again, there is simply nothing in the proposed regulations, nor has there ever been, that would indicate that the Department is to consider absence of harm or absence of facts which, if they existed, would make a criteria applicable.</p> <p>To the extent the regulations limit violators’ flexibility to negotiate on the basis of what they did <i>not</i> do, rather than the facts actually present in any given circumstance, such a limitation is desirable. And again, the new language eliminates, rather than creates, ambiguity, which will promote rather than hinder productive settlement negotiations</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>the criteria listed in Section 2591.3. Absence of harm, therefore, should and must mitigate the impact of those criteria.</p> <p>Likewise the new language states that inapplicability of any criteria shall not mitigate the effect of any relevant criterion. This language renders the Regulation incomprehensible. The criteria listed in Section 2591.3 are intended to assist the Department in determining whether an enforcement action should be initiated and in setting an appropriate penalty. The presence or absence of certain criteria, as well as the degree of harm, are considered in doing so. There are no hard and fast formulae to the calculation. Rather, the Department will set a penalty, for example, by weighing the various factors and applicable criteria. Where an important criterion does not apply, the Department may decide to reduce the penalty. The sentence added to Section 2591.4(a), however, would prevent the Department from doing so.</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>As these Regulations are intended to be used in connection with settlement negotiations, the Regulations must be flexible to allow the Department maneuverability. Language that eliminates flexibility will hamper the Department in negotiations and cause confusion as to how to apply the Regulations. This ambiguity would, in turn, make the Regulations less useful, and unnecessary. Accordingly, we strongly urge that the proposed last sentence in Section 2591.4(a) be eliminated.</p> <p><u>3. THE REGULATIONS ARE UNNECESSARY</u></p> <p><i>The revisions have not improved the clarity or necessity of the Regulations. The Regulations will not accomplish the stated purpose of increasing uniformity of settlements. Therefore, the Regulations do not meet the Government</i></p>	<p>The comment is not addressed to language that has been changed with the 15-day notice. Nonetheless, the Administrative Procedure Act's necessity standard is satisfied by Ins. Code § 12921.1, subd. (a), para. (7), which mandates the proposed regulations. Also, although the regulations do not purport to accomplish perfect uniformity in enforcement actions and settlements, there is no requirement that they do so. They will, however, provide for greater uniformity than presently exists.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p><i>Code's standard of necessity.</i></p> <p>As we pointed out in our previous comments, the Regulations require the Department to consider specified criteria, the Department may disregard those same criteria and add others if he sees fit. This reflects the present situation in which the Department has total discretion to bring an enforcement action and determine the appropriate penalty. As the factors set forth in the Regulations are not mandatory, they would not provide uniformity in enforcement actions and settlements. Revisions to Section 2591.4 do not address this concern, and therefore we reiterate that the Regulations do not meet the Government Code's standard of necessity.¹⁰</p> <p><u>4. THE REGULATIONS IMPROPERLY EXPAND THE CONCEPT OF WILLFULNESS</u></p> <p><i>The revisions have altered</i></p>	<p>This comment is not addressed to language that has been changed for the 15-day notice. The commenter's concerns referenced here are addressed exhaustively above. Nonetheless, any inconsistencies with existing law are resolved by the following language in Section 2591.1 of the proposed regulations: "To the extent that the provisions of this article conflict with the provisions of any statute or other regulation that more specifically</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p><i>language regarding “knowledge” or “willfulness” but have not remedied the basic flaw. The Regulations would still attribute knowledge and willfulness to the insurer absent evidence of the insurer’s specific intent to commit the violation. The factors as presently written therefore violate the Government Code standard of consistency.</i></p> <p>Section 2591.3(d)(1)(B)-(E) attribute knowledge or willfulness to the insurer without evidence of the insurer’s actual knowledge or willfulness. As explained in our previous comments, this contradicts case law discussing standards for knowledge and willfulness. Revisions to subsection (d) have not remedied this problem. Therefore, to avoid unfairness and inconsistency with law, the Regulations should be revised to attribute knowledge or willfulness only where evidence</p>	<p>the provisions of any statute or other regulation that more specifically addresses a particular violation, this article shall be inapplicable.”</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>exists that the insurer itself committed the violation with knowledge of the act and its unlawfulness and with knowledge of its probable consequences.</p> <p><u>5. CONCLUSION</u></p> <p>Revisions to the Regulations have not addressed our fundamental concerns that they lack authority, are inconsistent with law, unclear and unnecessary. In addition, they are ill advised because they would constrain the ability of insurers and the Commissioner to make settlements. We reiterate our position that the Regulations should be withdrawn as a whole. If the Regulations are to remain in effect, the revisions should be altered as described above.</p>	<p>The Department declines to take action on the basis of this comment, for the reasons stated above.</p>
Cinda Smith Counsel The GEICO Companies 5260 Western Avenue Chevy Chase, MD		<p>I write on behalf of Government Employees Insurance Company, GEICO General Insurance Company, GEICO Casualty Company, and GEICO Indemnity Company ("GEICO") to provide GEICO's comments to the revised text of</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
<p>20076 (301) 986-3568 (Telephone) (301) 718-5207 (Fax)</p> <p>Comments submitted via e-mail September 8, 2003</p>	2591	<p>RH02023676 concerning Enforcement Actions and Penalties.</p> <p>Section 2591, the Preamble to the regulation, states that the regulation Will apply to the statute pertaining to violations of statutes or Regulations which are discovered in the course of consumer complaints and that statute requires the commissioner to establish a list of criteria to determine which violations by insurers should be pursued through enforcement action. However, such no list is established by this proposed regulation. Without the guidance intended by the legislature and specifically included in the statute, insurers are left to guess what violations will lead to an enforcement action. Since the legislature clearly intended insurers to be on notice of which violations would lead to an enforcement action, the list should be included.</p>	<p>If the concern is that the list is not an exclusive list, there is no requirement that it be so, and the commenter does not identify any authority to support such a requirement. Essentially, this comment contends that the Legislature intended for insurers to be notified of which violations will lead to an enforcement action. A review of the language of Insurance Code section 12921.1(a)(7), however, reveals that, contrary to the commenter’s suggestion, the Legislature never said it wanted insurers to be “on notice of which violations would lead to an enforcement action.” Rather, the Legislature mandated that the Commissioner promulgate criteria to determine when the circumstances surrounding a particular violation are so egregious that an enforcement action and penalty should be imposed. Thus, this raises an important distinction between what the commenter believes was the Legislature’s intent, and what the plain language of Section 12921.1(a)(7) actually mandates. The Commissioner is authorized, pursuant to Section 12921.1(a)(7) to adopt criteria. Contrary to the contention of this comment, the mandate was not to list violations that would lead to an enforcement action, without regard to the specific factual nature of the violation itself. Additionally, this comment contends that, despite the fact that the proposed regulation says it provides a list of criteria to determine which violations should lead to an enforcement action, the regulations do not provide a list of criteria. On the contrary, proposed regulation Section 2591.3 expressly lists the criteria that will be used to determine whether a violation should be pursued through an enforcement action and to determine an appropriate penalty.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.1(b)	<p>The preamble also specifies that the article shall also apply to actions arising from findings generated by other regulatory activities that allege violations of the same statutes or regulations, including, but not limited to market conduct examinations. However, a regulatory structure is already in place for enforcement actions resulting from market conduct examinations. To allow enforcement actions to result from market conduct examinations under this rubric appears that it would allow consumer complaint investigators to repeat the work performed by market conduct field examiners. This appears to needlessly add to the task of consumer complaint investigators. In addition, to require both Department of Insurance and insurer personnel to respond to the same issue repeatedly will increase the cost to both the Department and to insurers.</p> <p>Despite the statement contained in the</p>	<p>The Commissioner has considered this comment and rejects it. The comment does not expand upon its assertion that “a regulatory structure is already in place for enforcement actions arising from market conduct examinations.” In fact, the commenter is incorrect, to the extent that she suggests that there are regulations that provide instructions as to when to conduct enforcement actions as a result of any market conduct examination. The proposed regulations fill this void by specifically creating a list of criteria to apply when deciding whether to conduct an enforcement action, based upon the findings of a market conduct exam. Moreover, the proposed regulations inject efficiency and clarity into the process by ensuring that investigations of consumer complaints and enforcement actions based upon market conduct examinations will operate in a consistent and cohesive fashion. The same regulations will be applicable to the work of consumer complaint investigations as well as those market conduct examinations that are sufficiently serious as to require an enforcement action. The proposed regulations will not impose new duties upon consumer complaint investigators. Rather, the regulations simply inform the public as to the kinds of considerations that the Department will apply internally, when deciding whether a consumer complaint or market conduct examination reveals violations so serious that an enforcement action is necessary. For these reasons, the proposed regulations will not increase the cost to the Department or insurers in responding to a consumer complaint. If anything, the proposed regulations will lessen that cost, while at the same time ensuring more consistent treatment of consumer complaints and market conduct issues.</p> <p>The Commissioner has considered this comment and rejects it. The preamble clearly states that this article applies to findings generated by</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.2	<p>preamble to the effect that the Article will apply to actions generated by other regulatory activities, including market conduct examinations, section 2591.1(b)(2) states that regulatory activity such as market conduct examinations or market conduct examination reports does not constitute an enforcement action. This statement is confusing as to the intended application of the proposed regulation.</p> <p>Section 2195.2 has now been amended so as to allow for the recovery of attorney fees. Since the insurance industry funds the insurance department through the payment of premium taxes, fees and assessments, it already underwrites the cost of Department attorneys in</p>	<p>preamble clearly states that this article applies to findings generated by regulatory activities, such as market conduct exams. Section 2591.1(b)(2) delineates the difference between a “market conduct exam” which generates findings, and an “enforcement action,” which is the administrative act of signing a formal pleading or settlement document to initiate or complete the hearing process. The language was added in order to clarify the distinction between the relatively rare situation where an enforcement action becomes necessary and the more routine occurrence of market conduct examinations. In fact, the American Insurance Association points out in its comment dated September 8, 2003, that the Commissioner’s modification to the Preamble removes any ambiguity regarding the difference between a market conduct examination and an enforcement action. As this regulation makes clear, not every market conduct examination will lead to an enforcement action. In fact, an enforcement action will only occur in those market conduct examinations that present findings of sufficient seriousness that the criteria listed in Section 2591.3 weigh in favor of imposing a fine through a formal settlement, or filing a notice of noncompliance or similar administrative legal pleading.</p> <p>The Commissioner has considered the comment and respectfully rejects it. The commenter is incorrect in stating that the “insurance industry funds the insurance department through the payment of premium taxes, fees and assessments....” Premium taxes do not fund the Department. “Fees and assessments” may, in part, fund the department, but they also go into the California’s General Fund. To allow recovery of additional attorney fees would not amount to a “duplicative assessment” as the commenter suggests. The insurance industry does not have a legitimate argument that just because they already are required by law to pay their taxes, fees, etc. they</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		large part. To allow the recovery of additional attorney fees would amount to a duplicative assessment.	<p>because they already are required by law to pay their taxes, fees, etc., they are now entitled to break the law and not have to pay a penalty for the violations just because they have already paid their dues. There is statutory authority for the Department to recover enforcement costs or attorney's fees from an insurer against whom an enforcement action has been taken. The reference note to section 2591.2 includes both CIC 12921, as well as the Department's rulemaking authority, CIC section 12921.1. Section 12921.1 expressly grants the Department authority to write regulations concerning consumer complaints. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department's authority to promulgate regulations which apply to other investigations of insurer conduct where the Department has inherent authority to implement its regulatory criteria. <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, "[The Commissioner's] powers are not limited to those expressly conferred by statute; 'rather, '[it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.'" (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that "[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter." (§ 1861.05, subd. (a).) (Italics added.)" <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.4	Section 2195.4 states that "absence of harm does not mitigate the effect of any criteria...." We are confused by the intent of this new language. The section also provides that the Department may consider matters not listed. How are insurers to know what sorts of matters may be considered?	<p>California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute. Section 2591 expressly recognizes that the regulations are to be used for settlement purposes. The reference note to section 2591.2 includes CIC 12921. Section 12921(b)(4) specifically states that "[I]n an administrative action to enforce the provisions of this code and other laws regulating the business of insurance in this state, any settlement is subject to....: a settlement may include the sanctions provided by this code or other laws regulating the business of insurance in this state, except that the settlement may include <i>attorney's fees, costs of the department in bringing the enforcement action, and future costs of the department to ensure compliance with the settlement agreement</i>" (emphasis added). Since it is intended that the provisions of section 2591 are appropriate for determining the penalty imposed in those cases that are resolved through <i>settlement</i> authority exists to recover enforcement costs or attorney's fees from an insurer against whom an enforcement action has been taken. Therefore, no change will be made.</p> <p>We appreciate the commenter's candor in indicating that it is not the new language itself in Section 2195.4 (for the language is clear) but the intent of the language which is confusing. The intent of the language is to preclude an interpretation of the regulations which would enable violators to argue that criteria that are applicable in a given case, because there are present certain affirmative facts that satisfy those criteria, should somehow be made less important or be given less consideration on the basis of there <i>not</i> being facts present which would implicate some other criterion, namely, as with, of the violation, one of the indicators of</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>GEICO thanks you for the ability to participate in the comment process Regarding this proposed new regulation. We hope our comments are helpful.</p>	<p>other criterion, namely severity of the violation, one of the indicators of which criterion is extent of harm. Perhaps the intent of the language is not immediately apparent because the possibility that someone might actually make such an argument seems implausible.</p> <p>Extent of harm is an indicator of the severity of the violation criterion; however, in order for this indicator to be operative, there must be facts indicating harm. Absence of such facts, on the other hand, simply means that this indicator is not triggered; it does not mean that an insurer committing a violation that is otherwise severe is essentially to be rewarded just because there has been no showing of harm. If the regulations indicated otherwise, insurers could be incentivized to commit violations in instances where there could be no such showing, if they thought they could predict that such violations would not be subject to enforcement actions or stiff penalties.</p> <p>There are mitigating factors in the proposed regulations, but they in each case are applicable only when affirmative facts trigger those criteria.</p> <p>Finally, it is true that Section 2591.4 of the amended text of the proposed regulations indicates that the Department may consider matters not listed in Section 2591.3. However, the text also provides that any such unlisted considerations will be stated during any settlement negotiations; insurers will therefore have a means of knowing all the sorts of matters that are being considered.</p> <p>It is true that insurers may not always be able to know in advance what other considerations may be taken into account. However, it is not necessary, or necessarily desirable, that they should always be able to know. The Department has made every effort to include in Section 2195.3 all criteria that can at present be envisaged would ever come into play. It is possible, nonetheless, that unforeseen circumstances may</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>make consideration of additional factors appropriate. To the extent this is the case, it is necessary that the regulations allow the Department adequate flexibility to consider such factors. Furthermore, it is not the primary goal of these regulations to let insurers know in advance every possible consideration that may obtain in the Department's determinations as to whether to pursue an enforcement action and as to the appropriate amount of the penalty, although the regulations do to a large degree accomplish this goal. It is enough for insurers to know that they are to avoid all violations of the Insurance Code, regardless of whether or not they believe they can predict which violations will be pursued through enforcement action.</p>
<p>Karen Colonna Assistant General Counsel American International Companies DBG Legal</p>		<p>This letter is submitted on behalf of the member companies of American International Group, Inc. (collectively "AIG"). We have reviewed the August 22, 2003 notice of the changes to the proposed regulations regarding enforcement actions and penalties.</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
<p>Services 175 Water Street, 18th Floor New York, New York, 10038 (212) 458-2542</p> <p>Comments submitted on behalf of AIG via email on September 5, 2003</p>	2591.4(a)	<p>The following is our recommended change to the language proposed under Section 2591.4(a). We feel that the last sentence of this subsection (a) should be amended to read as follows:</p> <p>he inapplicability of one or more criteria may not mitigate the effect of any of the relevant criterion.”</p> <p>We believe the currently proposed language: “Neither inapplicability of one or more criteria nor absence of harm shall mitigate the effect of the relevant criterion” is unclear in its meaning. This language can be read to mean that the Department cannot consider “absence of harm” as a mitigating factor, even though the clear intent of the proposed regulations is for the Department to consider the degree of harm and various other mitigating factors. In addition, the currently proposed language may also be read to mean that the Department would be prohibited from considering the inapplicability of one or more criteria</p>	<p>The language proposed by the commenter is itself unclear. Does “may not mitigate” mean “shall not,” or does it mean “may or may not”? Including this language would likely cause the regulations to run afoul of the Administrative Procedure Act’s clarity standard. Accordingly the language will not be changed.</p> <p>The language is perfectly clear. Not only can it be read, but the <i>only</i> way it can be read is, “to mean that the Department cannot consider ‘absence of harm’ as a mitigating factor.” There is no basis for the commenter’s implied assertion that this sentence is somehow at odds with the “clear intent” of the regulations. It is true that there are mitigating factors in the regulations (viz., § 2591.3(h), (b)(2), and (f)(2) in the amended text of the proposed regulations), but they are in each case based on the presence of affirmative facts which satisfy those criteria.</p> <p>Extent of harm is an indicator of the severity of the violation criterion; however, in order for this indicator to be operative, there must be facts indicating harm. Absence of such facts, on the other hand, simply means that this indicator is not triggered; it does not mean that an insurer committing a violation that is otherwise severe is essentially to be rewarded just because there has been no showing of harm. If the regulations indicated otherwise, insurers could be incentivized to commit violations in instances where there could be no such showing, if they thought they could predict that such violations would not be subject to enforcement actions or stiff penalties.</p> <p>Again, there is simply no basis in fact for the commenter’s assertion that it is the “intent” of the regulations that inapplicability of a criterion be considered a mitigating factor. This is why the commenter is unable to cite language to this effect in the text of the regulations. There are mitigating factors in the proposed regulations, as noted above, but they in</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>as a mitigating factor. Again, this conflicts with the intent of the proposed regulations. We believe that the language we propose along with the first two currently proposed sentences of Section 2591.4(a) would allow the Department the flexibility to weigh each criterion separately, but still consider possible mitigating factors.</p> <p>If you have any questions regarding the above, do not hesitate to contact me at (212) 458-2542.</p>	<p>each case are applicable only when affirmative facts trigger those criteria.</p>
<p>American Insurance Association</p> <p>Mr. Bill Gausewitz American Insurance Association 980 Ninth Street, Suite 2060</p>		<p>On behalf of the American Insurance Association, I am writing to comment upon the proposed changes to the above-captioned regulations. Pursuant to the California Administrative Procedures Act, I will comment only upon the variations between the proposed revised regulations of August 22, 2003 and the original proposal of November 1, 2002. Except as stated explicitly</p>	

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		cited do not authorize recovery of attorney fees. As this provision lacks authority, we urge that it be deleted.	<p><i>Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, “[The Commissioner’s] powers are not limited to those expressly conferred by statute; “rather, ‘[it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.’” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (Italics added.)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute. The cases cited do not stand for the specific authority to recover attorney fees, but the inherent authority to implement regulations to do so. Section 2591 expressly recognizes that the regulations are to be used for settlement purposes. The reference note to section 2591.2 includes CIC 12921. Section 12921(b)(4) specifically states that “[I]n an administrative action to enforce the provisions of this code and other laws regulating the business of insurance in this state, any settlement is subject to...: a settlement may include the sanctions provided by this code or other laws regulating the business of insurance in this state, except that the</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.4(a)	<p>Section 2591.4(a), Harm: The revised regulations provide that “[n]either inapplicability of one or more criteria nor absence of harm shall mitigate the effect of any relevant criterion.” The phrase “nor absence of harm” makes the regulation internally inconsistent and therefore lacking in required clarity. Proposed §2591.3(b) specifically says that the severity of a violation is a factor in assessing penalty. Section 2591.3(b)(1)(A) explicitly says that the “extent of harm” is an appropriate consideration in determining severity and, therefore, in determining the amount of a penalty. Saying in §2591.4(a) that the “absence of harm”</p>	<p>settlement may include <i>attorney’s fees, costs of the department in bringing the enforcement action, and future costs of the department to ensure compliance with the settlement agreement</i>” (emphasis added). Since it is intended that the provisions of section 2591 are appropriate for determining the penalty imposed in those cases that are resolved through <i>settlement</i> authority exists to recover enforcement costs or attorney’s fees from an insurer against whom an enforcement action has been taken. Therefore, no change will be made.</p> <p>There is no inconsistency. Nothing in Section 2591.3 indicates that lack of harm is to mitigate the effect of any relevant criterion, nor is there a requirement that the Department consider lack of applicability of other criteria, which is why the commenter can point to no specific language to this effect in Section 2591.3.</p> <p>The commenter quotes accurately from the language of Section 2591.3, but then draws a conclusion not based on the quoted language. It simply does not follow from the cited material that absence of harm is to mitigate the effect of any relevant criterion.</p> <p>It is true that severity of the violation is a criterion. It is also true that one of the indicators of this criterion is extent of harm (§2591.3(b)(1)(A)). Absence of harm, however, is not an indicator. The sentence in Section 2591.4, subdivision (a), that is complained of here is therefore not inconsistent with the severity of the violation criterion. The sentence is apparently necessary, though, in order to prevent insurers from imputing to the regulations the unintended meaning that absence of harm is to be considered a mitigating factor. It is not. The only possible meaning</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>shall not mitigate the effect of the criterion is inconsistent §2591.3(b)(1)(A). We respectfully urge that this newly-added provision of §2591.4(a) be deleted.</p> <p>Thank you for your consideration of these comments.</p>	<p>—and the intended meaning—of the sentence complained of is that extent of harm, in the proposed regulations, can never be considered as a mitigating factor.</p> <p>Extent of harm is an indicator of the severity of the violation criterion; however, in order for this indicator to be operative, there must be facts indicating harm. Absence of such facts, on the other hand, simply means that this indicator is not triggered; it does not mean that an insurer committing a violation that is otherwise severe is essentially to be rewarded just because there has been no showing of harm. If the regulations indicated otherwise, insurers could be incentivized to commit violations in instances where there could be no such showing, if they thought they could predict that such violations would not be subject to enforcement actions or stiff penalties. For this reason the extent of harm trigger and the complained of sentence harmonize to indicate that the extent of harm trigger can never be a mitigating factor but, when operative, can only be an aggravating factor. This is an appropriate, and the intended, result. Violators are not to reap a windfall just because there happens not to be a showing of facts indicating particular harm arising from their violations of the law</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
<p>Mr. Samuel Sorich</p> <p>Association of California Insurance Companies 1121 L Street, Suite 406 Sacramento, CA 95814-3943</p> <p>September 8, 2003 Written submission via e-mail</p>	<p>2591.1(d)</p>	<p>The Association of California Insurance Companies (ACIC) is an association of property/casualty insurance companies. There are 237 ACIC member companies doing business in California. ACIC members are responsible for approximately 34% of all property/casualty insurance premiums written in California. ACIC is an affiliate of the National Association of Independent Insurers.</p> <p>This statement addresses the August 22, 2003 revised text of proposed regulations for enforcement actions and penalties. This statement supplements the written statement which ACIC submitted on December 17, 2002 and the comments which ACIC made at the December 17, 2002 public hearing on the proposed regulations.</p> <p>Section 2591.1(d) – Application of Regulations to Administrative or Judicial Proceedings</p> <p>The August 22 revision to Section</p>	<p>This commenter argues that the revision to Section 2591.1 creates an uncertainty as to whether the regulations absolutely do not apply to administrative proceedings. The Commissioner has considered the comment and rejects it. In fact, the changes to this regulation enhance certainty and clarity, by describing more clearly the circumstances under</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>2695.1(d) removed language which clearly stated that the regulations “do not apply” to administrative orders, judicial decisions or settlement conferences ordered pursuant to the Administrative Procedure Act. The deleted language should be restored. Removal of the language creates an uncertainty. According to the August 22 revised text, the regulations “are not intended” to be consulted by hearing officers or judges, but there is no clear statement that the regulations absolutely do not apply to administrative proceedings.</p> <p>In order to achieve greater clarity and to provide hearing officers with clear direction, ACIC recommends that the language deleted from Section 2691.1(d) be put back into the section. When the language is restored, the word decision” should be replaced with the word “proceeding.” The inapplicability of the regulations pertains not just to the ultimate judicial decision, but to any stage of a judicial proceeding.</p>	<p>certainty and clarity, by describing more clearly the circumstances under which these regulations apply.</p> <p>The revision to Section 2591.1 is designed to provide a clear indication of this regulation’s purpose. Specifically, this proposed regulation expressly states that it is not intended for use by a hearing officer, judge or trier of fact in connection with an action brought by the Department. The regulations were revised in order to make this intention more clear. Indeed, the current revised language also achieves the clarity that the commenter requests by including language that more clearly and broadly defines the context in which the regulations are not intended to be applied by hearing officers and judges. Specifically, this is accomplished by removing the phrase “judicial decision” and inserting broader language, which prohibits a “hearing officer, judge or trier of fact” from even consulting these regulations “in connection with an action brought by the Department.” (Emphasis added.) Thus, the revisions to the regulation describe the circumstances under which these regulations are intended for use with much more clarity.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.2	<p><u>Section 2591.2 – Attorney’s Fees and Enforcement Costs</u></p> <p>The August 22 revised text changed the last sentence of Section 2591.2 to allow the Department of Insurance to recover attorney’s fees as part of the enforcement costs that are recovered from an insurer. There is no statutory authority for the Department of Insurance to recover enforcement costs or attorney’s fees from an insurer against whom an enforcement action has been taken.</p> <p>Insurance Code §736 requires an insurer to pay for the costs of the Department of Insurance’s market conduct examination of an insurer. However, §736 cannot be the basis for requiring an insurer to pay for the costs of an enforcement action because Section 2591.1(b)(2) of the proposed regulations states that a market conduct examination is not an enforcement action.</p> <p>The proposed regulations are intended to apply to the nineteen</p>	<p>The Commissioner has considered the comment and respectfully rejects it. There is statutory authority for the Department to recover enforcement costs or attorney’s fees from an insurer against whom an enforcement action has been taken. The reference note to section 2591.2 includes both CIC 12921, as well as the Department’s rulemaking authority, CIC section 12921.1. Section 12921.1 expressly grants the Department authority to write regulations concerning consumer complaints. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department’s authority to promulgate regulations which apply to other investigations of insurer conduct where the Department has inherent authority to implement its regulatory criteria. <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, “[The Commissioner’s] powers are not limited to those expressly conferred by statute; “rather, ‘[it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.’” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (Italics added.)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(b) 2(1)(A)	<p>penalties statutes listed in Section 2591.1(c). None of these statutes includes a provision that authorizes the Department to recover enforcement costs or attorney's fees.</p> <p>The last sentence of proposed Section 2591.2 violates the regulatory standard of authority, as that standard is defined in Government Code §11349. The sentence should be deleted.</p> <p><u>Section 2591.3(b)(1)(A) – Actions and Penalties Not Based on Consumer Complaints</u></p> <p>The August 22 revision added Section 2591.3(b)(1)(A). In describing the severity criterion, proposed Section 2591.3(b)(1)(A) states that consideration may be given to harm revealed through a consumer complaint “or otherwise brought to</p>	<p>authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute. Section 2591 expressly recognizes that the regulations are to be used for settlement purposes. The reference note to section 2591.2 includes CIC 12921. Section 12921(b)(4) specifically states that “[I]n an administrative action to enforce the provisions of this code and other laws regulating the business of insurance in this state, any settlement is subject to...: a settlement may include the sanctions provided by this code or other laws regulating the business of insurance in this state, except that the settlement may include <i>attorney’s fees, costs of the department in bringing the enforcement action</i>, and future costs of the department to ensure compliance with the settlement agreement” (emphasis added). Since it is intended that the provisions of section 2591 are appropriate for determining the penalty imposed in those cases that are resolved through <i>settlement</i> authority exists to recover enforcement costs or attorney’s fees from an insurer against whom an enforcement action has been taken. Therefore, no change will be made.</p> <p>The Commissioner has considered and rejects it, insofar as this comment contends that the proposed regulation violates the authority standard because it applies to more than mere violations of statutes discovered through the investigation of consumer complaints. The Commissioner’s authority comes not only from Insurance Code section 12921.1(a)(7) and the consumer complaint statutes, but also from the inherent authority derived from other provisions of the code that designate a range of penalties with no guidelines for selecting a penalty from within the range.</p> <p>Consumer harm may be brought to the attention of the Department through circumstances which are not related to a consumer complaint</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>the attention of the Department.” The inclusion of this quoted phrase is not authorized by the Insurance Code</p> <p>As ACIC explained in our December 17, 2002 written statement, Insurance Code §1291.1(a)(7) provides the specific statutory authority for the proposed regulations. Insurance Code §12921.(a)(7) “pertains to violations of statutes and regulations which are discovered through the investigation of consumer complaints.” The authority granted to the Department of Insurance by §12921.1(a)(7) to develop criteria for enforcement actions and penalties does not extend to matters that are brought to the attention of the Department by activities that are not related to consumer complaints. In order to comply with the regulatory standard of authority, Section 2591.3(b)(1)(A) should be limited to harm revealed through a consumer complaint. The phrase “or otherwise brought to the attention of the Department” should be deleted.</p>	<p>through circumstances, which are not related to a consumer complaint. For instance, as these regulations anticipate in Section 2591(b), “other Department investigations, examinations, or reviews of insurer conduct” may present evidence of consumer harm. The Commissioner is given broad authority to investigate such harm and consider the evidence of such harm in deciding whether or not to bring an enforcement action or assess a penalty.</p> <p>The comment suggests that the Department lacks authority to make these regulations applicable to cases other than those that begin through the complaint investigation program described in Insurance Code section 12921.1. The Commissioner has considered the comment and rejects it.</p> <p>Subdivision (b) of proposed regulations section 2591 acknowledges that these regulations are intended to apply to more cases than simply those cases subject to Insurance Code section 12921.1(a)(7). Indeed, the Reference provision and section 2591.1 of the proposed regulations list the penalty provision statutes, which these regulations will implement, interpret and make specific. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department’s authority to promulgate regulations which apply to other investigations of insurer conduct where the Department has inherent authority to implement its regulatory criteria.</p> <p>The penalty statutes listed in the Reference provision and section 2591.1 give the Commissioner authority to impose a penalty from within a range. For example, Insurance Code section 1858.07 authorizes the Commissioner to impose a penalty “not to exceed” \$5,000 for a non-willful violation and “not to exceed” \$10,000 if the violation is willful. Insurance Code section</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>When Section 2591.3(b)(1)(A) is further revised, it should be made clear that the reference to consumer complaints is specific to complaints that are justified since only justified complaints are the proper basis for enforcement actions and penalties. Therefore, ACIC recommends that the word “justified” should be added to modify “consumer complaint” in Section 2591.3(b)(1)(A).</p>	<p>“not to exceed” \$10,000 if the violation is willful. Insurance Code section 12921, subdivision (a) requires the Commissioner to enforce the provisions of the Insurance Code and other laws relating to the business of insurance in this state. The Commissioner has inherent power to implement, interpret and make specific the manner in which these penalty ranges will be applied in practice.</p> <p><i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, “[The Commissioner’s] powers are not limited to those expressly conferred by statute; ‘rather, [it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.’” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (Italics added.)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute.</p> <p>Here, the proposed regulations will apply to statutes which authorize the Commissioner to seek a penalty “not to exceed” a certain amount. (See,</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>e.g., Ins. Code sections 1858.07 & 10140.5.) It is necessary to promulgate regulations for settlement purposes insofar as the statutes referenced in the proposed regulations authorize the Commissioner to impose penalties within a range, and therefore the Commissioner has inherent authority to create a regulatory scheme to decide appropriate penalties within that range. Furthermore, each agency has inherent (as well as statutory) power to settle cases prior to a hearing, in a manner in which the parties see fit. (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114.)</p> <p>Government Code section 11415.60 recognizes that “[a]n agency may formulate and issue a decision by settlement, pursuant to an agreement of the parties, without conducting an adjudicative proceeding. Subject to subdivision (c), the settlement may be on any terms the parties determine are appropriate.” Subdivision (c) states, in part, “The terms of a settlement may not be contrary to statute or regulation, except that the settlement may include sanctions the agency would otherwise lack power to impose.”</p> <p>Therefore, the Commissioner has broad discretion to adopt rules and regulations as necessary to promote the public welfare. The proposed regulations concern a number of statutes that give the Commissioner the power to impose penalties within a range after a hearing, but the statutes are silent regarding where the appropriate penalty is within the range. We also know that agencies are empowered to settle cases prior to hearing, and that the settlement may include sanctions which do not violate public policy that the agency would otherwise lack the power to impose. It is reasonable for the Commissioner to conclude that, when settling cases, he will use the statutory penalty ranges as a guideline for deciding what sanctions to impose at settlement. Moreover, the Commissioner’s broad discretion to adopt rules and regulations that “may</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.3(f)(2)	<p><u>Section 2591.3(f)(2) – Insurer’s Cooperation</u></p> <p>The August 22 revision attempts to clarify the nature of an insurer’s actions that reflect the insurer’s compliance record. Further clarification is needed. As proposed, the section would consider correction of “any” non-complaint activity. The word “the” should be substituted for the word “any.” This change will make it clear that the criterion relates to the specific matter that was the subject of a consumer complaint.</p>	<p>Commissioner’s broad discretion to adopt rules and regulations that “may fairly be implied from the statute granting the powers” authorizes him to create guidelines/criteria for enforcement and penalty assessment. (See, generally, <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825.)</p> <p>The authority to adopt these regulations may be fairly implied from those statutes that recognize the agency’s inherent power to settle cases “on any terms the parties determine are appropriate.” Additionally, the authority to adopt these regulations may be fairly implied from those statutes that designate a penalty range that may be imposed after a hearing.</p> <p>The commissioner has considered this comment and rejects it. The compliance record criterion allows consideration of the insurer’s past non-compliant behavior as well as any mitigating corrective action taken by the insurer or the insurer’s failure to take corrective action when indicated. The commissioner should not be limited to reviewing only a specific type of noncompliance when reviewing an insurer’s compliance history. This criterion provides the commissioner with the necessary flexibility to put the violation into context with the overall compliance behavior of the insurer, which is particularly necessary in determining whether an enforcement action is necessary to encourage future compliance by the insurer or whether the noncompliance was an aberration that, once corrected, is not likely to be repeated.</p> <p>To limit compliance history to only the type of noncompliance in the current complaint defeats the purpose of this criterion and could be read as providing an incentive for insurers to be creative in their violations. Insurers are to avoid all violations of the Insurance Code.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.4(a)	<p><u>Section 2591.4(a) – Absence of Harm</u></p> <p>The August 22 revised text added a final sentence to Section 2591.4(a). The sentence provides that the absence of harm shall not mitigate the effect of any relevant criteria. This provision is inconsistent with proposed Section 2591.3(b)(1)(A), which expressly directs the Department to consider “the extent of harm.” In order to comply with the regulatory standard of consistency, as that standard is defined in Government Code §11349, the last sentence of proposed Section 2591.4(a) should be deleted.</p>	<p>There is no inconsistency. Nothing in Section 2591.3 indicates that lack of harm is to mitigate the effect of any relevant criterion, nor is there a requirement that the Department consider lack of applicability of other criteria, which is why the commenter can point to no specific language to this effect in Section 2591.3.</p> <p>The commenter quotes accurately from the language of Section 2591.3, but then draws a conclusion not based on the quoted language. It simply does not follow from the cited material that absence of harm is to mitigate the effect of any relevant criterion.</p> <p>It is true that severity of the violation is a criterion. It is also true that one of the indicators of this criterion is extent of harm (§2591.3(b)(1)(A)). Absence of harm, however, is not an indicator. The sentence in Section 2591.4, subdivision (a), that is complained of here is therefore not inconsistent with the severity of the violation criterion. The sentence is apparently necessary, though, in order to prevent insurers from imputing to the regulations the unintended meaning that absence of harm is to be considered a mitigating factor. It is not. The only possible meaning — and the intended meaning — of the sentence complained of is that extent of harm, in the proposed regulations, can never be considered as a mitigating factor.</p> <p>Extent of harm is an indicator of the severity of the violation criterion; however, in order for this indicator to be operative, there must be facts indicating harm. Absence of such facts, on the other hand, simply means that this indicator is not triggered; it does not mean that an insurer committing a violation that is otherwise severe is essentially to be rewarded just because there has been no showing of harm. If the regulations indicated otherwise, insurers could be incentivized to commit violations in instances where there could be no such showing, if they</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.4(c)	<p><u>Section 2591.4(c) – List of Criteria</u></p> <p>Insurance Code §12921.1(a)(7) requires the insurance commissioner to adopt regulations that contain “a list of criteria” to determine whether to undertake enforcement actions and to guide the setting of penalties. The August 22 revision of proposed Section 2591.4(c) conflicts with the authority granted to the insurance commissioner by §12921.1(a)(7). The revision would allow the Department of Insurance to consider</p>	<p>thought they could predict that such violations would not be subject to enforcement actions or stiff penalties. For this reason the extent of harm trigger and the complained of sentence harmonize to indicate that the extent of harm trigger can never be a mitigating factor but, when operative, can only be an aggravating factor. This is an appropriate, and the intended, result. Violators are not to reap a windfall just because there happens not to be a showing of facts indicating particular harm arising from their violations of the law.</p> <p>Incidentally, the consistency standard of the Administrative Procedure Act as outlined in the cited Gov. Code § 11349 does not apply here, and would not, even if the regulations were internally inconsistent, which, as has been pointed out, they are not. The consistency standard pertains to consistency with existing law.</p> <p>And contrary to the commenter’s assertion, Section 2591.3 of the proposed regulations is just such a list as is called for in Ins. Code § 12921.1(a)(7). If the concern is that the list is not an exclusive list, there is no simply no requirement that it be so, and the commenter does not identify any such requirement, in either the statute or its legislative history. Moreover, the regulations clearly provide that in the event that an unlisted criterion is used, the basis for this consideration will be stated during any settlement negotiations. Consequently, insurers will have a way of knowing what criteria are being used. Further, if the list of criteria were indeed an exclusive one, the Department would be deprived of the flexibility that is often necessary in order for settlement discussions to be productive. Finally, it is not the intent of the proposed regulations, or the statutes they implement, to give would-be violators</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
		<p>criteria that are not listed in the regulations. The ability to consider matters that are not listed in the regulations runs counter to the Legislature's intent that the Department's decisions should be guided by "a list." If consideration may be given to non-listed matters, the Legislature's goal of making sure that the Department's actions are guided by a specific list of criteria could be undermined. Moreover, insurers subject to the regulation will have no way of knowing what non-specified criteria could be used. In order to be consistent with the authority granted to the insurance commissioner by §12921.1(a)(7), proposed Section 2591.4(c) should be amended to exclude consideration of criteria that are not listed in the proposed regulations.</p> <p>ACIC appreciates the Departments of Insurance's consideration of these comments.</p>	<p>regulations, or the statutes they implement, to give would-be violators advice in advance as to which of their violations will or will not be pursued through enforcement actions or receive stiff penalties. Insurers are to avoid all violations of the Insurance Code.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTS	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
<p>Ms. G. Diane Colborn Vice President Regulatory Affairs Personal Insurance Federation of California 980 Ninth Street Suite 2030 Sacramento, CA 95814 (916) 442-6646</p> <p>September 8, 2003 Written submission via e-mail</p>	2591.2	<p>The Personal Insurance Federation of California submits these comments in response to the fifteen-day notice on the revised text of proposed regulations relating to enforcement actions and penalties. These comments are limited to the changes only. Our prior comments, dated December 17, 2002, are incorporated by reference.</p> <p>We would like to highlight the following two concerns with the changes to the regulations:</p> <p>Section 2591.2 provides that the Department may recover its costs associated with the enforcement action, <u>including but not limited to attorneys' fees</u>. We are not aware of any statutory authority, nor are any cited by the Department in the notice, for recovery of the Department's attorneys fees from the insurer. Neither Section 791.10 nor Section 12921.1 provide such authority.</p>	<p>The Commissioner has considered the comment and respectfully rejects it. First, the commenter states that section 791.10 does not provide such authority for recovery of the Department's attorney's fees from the insurer. Section 791.10 concerns adverse underwriting decisions; therefore, such comment does not address any aspect of this regulation. There is statutory authority for the Department to recover enforcement costs or attorney's fees from an insurer against whom an enforcement action has been taken. The reference note to section 2591.2 includes both CIC 12921, as well as the Department's rulemaking authority, CIC section 12921.1. Section 12921.1 expressly grants the Department authority to write regulations concerning consumer complaints. The fact that Insurance Code section 12921.1(a)(7) gives express authority to promulgate regulations concerning consumer complaints does not restrict the Department's authority to promulgate regulations which apply to other investigations of insurer conduct where the</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>Department has inherent authority to implement its regulatory criteria. <i>CalFarm v. Deukmejian</i> (1989) 48 Cal.3d 805, 825 is instructive. That case states, in part, “[The Commissioner’s] powers are not limited to those expressly conferred by statute; “rather, “[it] is well settled in this state that [administrative] officials may exercise such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as <i>may fairly be implied</i> from the statute granting the powers.’” (<i>Rich Vision Centers, Inc. v. Board of Medical Examiners</i> (1983) 144 Cal.App.3d 110, 114 [192 Cal.Rptr. 455], quoting <i>Dickey v. Raisin Proration Zone No. 1</i> (1944) 24 Cal.2d 796, 810 [151 P.2d 505, 157 A.L.R. 324].) The power to grant interim relief is necessary for the due and efficient administration of Proposition 103, and may fairly be implied from its command that “[no] rate shall ... <i>remain in effect</i> which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter.” (§ 1861.05, subd. (a).) (Italics added.)” <i>20th Century v. Garamendi</i> (1994) 8 Cal. 4th 216, 280 is another case involving similar issues. Both of these cases were in the context of Proposition 103. The California Supreme Court, in those cases, was describing the inherent authority of the Commissioner to implement a statutory scheme through regulation even when the statutory scheme did not give express authority to promulgate regulations to implement the statute. Section 2591 expressly recognizes that the regulations are to be used for settlement purposes. The reference note to section 2591.2 includes CIC 12921. Section 12921(b)(4) specifically states that “[I]n an administrative action to enforce the provisions of this code and other laws regulating the business of insurance in this state, any settlement is subject to...: a settlement may include the sanctions provided by this code or other laws regulating the business of insurance in this state, except that the settlement may include <i>attorney’s fees, costs of the department in bringing the enforcement action, and future</i></p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
	2591.4(a)	<p>Section 2591.4(a) has been revised to include the following additional sentence: “<u>Neither inapplicability of one or more criteria nor absence of harm shall mitigate the effect of any relevant criterion.</u>” This sentence lacks clarity and is internally inconsistent. How can a criterion be both inapplicable and relevant? Moreover, it is unclear why the total absence of harm should not be a mitigating factor. We recommend that this sentence be stricken for failure to meet both the clarity and necessity standards.</p> <p>Thank you for your consideration of these comments. If you have any questions regarding the comments please let us know.</p>	<p>costs of the department to ensure compliance with the settlement agreement” (emphasis added). Since it is intended that the provisions of section 2591 are appropriate for determining the penalty imposed in those cases that are resolved through <i>settlement</i> authority exists to recover enforcement costs or attorney’s fees from an insurer against whom an enforcement action has been taken. Therefore, no change will be made.</p> <p>The sentence is perfectly clear in that it is in plain English and can have only one meaning, as the commenter’s rhetorical question implies: “How can a criterion be both inapplicable and relevant?” Clearly, a criterion cannot be both inapplicable and relevant. The sentence is necessary to preclude an interpretation of the regulations — albeit a far-fetched interpretation — along the lines that the absence of facts which, if they were present, might make certain criteria relevant should itself be considered relevant for purposes of mitigating the effect of other criteria that are relevant by virtue of the existence of affirmative facts which satisfy those other criteria. The sentence complained of very clearly preempts this interpretation.</p> <p>For the commenter to say that it is unclear why absence of harm should not be a mitigating factor again indicates that the sentence is clear: Absence of harm is indeed not to be considered a mitigating factor.</p> <p>As to why the Department has elected to preclude absence of harm from being considered a mitigating factor, one reason is that <i>absence</i> of facts is simply never a relevant factor — aggravating <i>or</i> mitigating — in these regulations. There are mitigating criteria (viz., § 2591.3(h), (b)(2), and (f)(2) in the amended text of the proposed regulations), but they are in each case based on the presence of affirmative facts which satisfy those criteria.</p>

RH 02023676
Regulations for Enforcement Actions and Penalties
Summary and Response to Public Comments re Proposed Regulations

COMMENTER	SECTION	VERBATIM COMMENT (All mistakes in text appear in original)	CDI RESPONSE
			<p>As to why it is necessary to mention absence of harm specifically, Paragraph 2591.3(b)(1)(a) of the Amended Text of Regulation lists extent of harm as an indicator of the severity of the violation criterion. However, if one or more of the other indicators of this criterion is triggered (i.e., amount of underpayment of a claim), the criterion will receive no less consideration than it otherwise might simply by virtue of the fact that no particular harm arising from the violation has been brought to the attention of the Department. This provision reflects a judgment on the Department's part that a violation can indeed be severe without there necessarily having to be a showing of harm arising from it.</p>